SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1944

No. 953

JOHN F. X. FINN, AS TRUSTEE OF CHILDS COMPANY, PETITIONER,

vs.

BURTON C. MEIGHAN, JR., AS SUBSTITUTED TRUSTEE UNDER THE LAST WILL AND TESTAMENT OF WILLIAM T. WOOD, DECEASED

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

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[fol. 1]

IN UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

In the Matter of CHILDS COMPANY, Debtor

In Proceedings for Reorganization under Chapter X of the Bankruptcy Act—No. 82,868

BURTON C. MEIGHAN, JR., as Substituted Trustee under the Last Will and Testament of William T. Wood, Deceased, Petitioner-Appellee,

against

JOHN F. X. FINN, as Trustee of Childs Company, Respondent-Appellant

STATEMENT UNDER RULE XIII

This appeal is from an Order dated September 27, 1944, entered on October 2nd, 1944, by Hon. Edward A. Conger, in the United States District Court for the Southern District of New York, in voluntary proceedings for the reorganization of Childs Company under Chapter X of the Chandler Act. The Order appealed from granted the petition of Burton C. Meighan, Jr., as Substituted Trustee [fol. 2] under the Last Will and Testament of William T. Wood, Deceased, verified June 27, 1944, praying for an order adjudging that the term granted to Childs Company, the Debtor herein, by an indenture of lease dated July 31, 1922, as modified in certain respects by an agreement dated March 23, 1942, has terminated and come to an end, and further that the Trustee of the Debtor be ordered forthwith to surrender possession of the premises 1553 Broadway, New York City, to said Burton C. Meighan, Jr., Trustee as aforesaid.

Said petition of Burton C. Meighan, Jr., Trustee as aforesaid, by order to show cause dated July 6, 1944, was heard on July 25, 1944, and referred by Order of the United States District Court, dated July 26, 1944, to Hon. Robert P. Stephenson, as Special Master, to hear the proofs and arguments of the parties and to report his findings of fact and conclusions of law thereon. Said Robert P. Stephenson filed his Report as Special Master, including opinion and

findings of fact and conclusions of law, with the Clerk of the United States District Court on August 7, 1944, and recommended the granting of the petition of Burton C. Meighan, Jr., as Substituted Trustee as aforesaid, verified June 27, 1944.

The Order appealed from confirmed the said Report of the Special Master and adopted the Special Master's findings of fact and conclusions of law, and adjudged that the term granted the Childs Company by indenture of lease dated July 31, 1932, as modified in certain respects by an agreement March 23, 1942, covering the premises known as and by 1553 Broadway, Borough of Manhattan, New York City, came to an end and terminated on August 26, 1943, and directed John F. X. Finn, as Trustee of Childs Company, to surrender possession of said premises within thirty days from September 27, 1944, to said Burton C. Meighan, Jr., Substituted Trustee as aforesaid.

[fol. 3] On August 26, 1943, Childs Company filed in the United States District Court for the Southern District of New York a petition for voluntary proceedings for reorganization under Chapter X of the Bankruptcy Act. On the same day an order was made by the Hon. Edward A. Conger, approving said petition of the Debtor and appointing John F. X. Finn as trustee thereof.

In the aforesaid proceeding in the United States District Court for the Southern District of New York, Lorenz, Finn & Lorenz, Esqs., appeared for John F. X. Finn, as Trustee of Childs Company, the appellant herein, and Meighan & Necarsulmer, Esqs., appeared for Burton C. Meighan, Jr., as Substituted Trustee under the Last Will and Testament of William T. Wood, Deceased, the appellee. There has been no change of parties or attorneys since the commencement of this proceeding.

John F. X. Finn, as trustee of the debtor herein, the aggrieved party on this appeal from the Order of the District Court, dated September 27, 1944, filed notice of appeal therefrom on October 4, 1944, with the Clerk of the United States District Court for the Southern District of New York.

[fol. 4] IN UNITED STATES DISTRICT COURT, SOUTHERN DISTRICT OF NEW YORK

[Same Title]

ORDER TO SHOW CAUSE

Upon the annexed petition of Burton C. Meighan, Jr., Substituted Trustee under the Last Will and Testament of William T. Wood, Deceased, verified June 27, 1944, and sufficient reason appearing therefor, it is

Ordered that John F. X. Finn, trustee of the debtor herein, the debtor, and Securities and Exchange Commission show cause before me at Room 2003, United States Courthouse, Foley Square, Borough of Manhattan, City of New York, on the 18th day of July, 1944, at 10:30 o'clock in the forenoon, or as soon thereafter as counsel can be heard, why an order should not be granted herein:

1. Adjudging that the term granted by a certain indenture of lease dated July 31, 1922, made by and between Gramway Company, Inc., as landlord, and Childs Company, as tenant, and as modified in certain respects by an agreement dated the 23rd day of March, 1942, made by and between Burton C. Meighan, Jr., as Substituted Trustee under the Last Will and Testament of William T. Wood, Deceased (the successor of all the rights and privileges of the Gramway Company, Inc.), as landlord, and Childs Company, as tenant, has terminated and come to an end;

2. Authorizing and directing John F. X. Finn, as trustee of the debtor herein, and the said debtor to forthwith sur- [fol. 5] render possession of premises located at and known as 1553 Broadway, Borough of Manhattan, City, County and State of New York, to said Burton C. Meighan, Jr., as Substituted Trustee as aforesaid;

3. Granting to said petitioner such other and further relief as to the Court may seem proper in the premises; and it is further

Ordered that service of a copy of this order and of the petition upon which the same is based upon Lorenz, Finn & Lorenz, Esqs., attorneys for the trustee, George Zolotar, Esq., attorney for the Securities and Exchange Commission, and Barber & Grunden, Esqs., attorneys for the debtor, per-

sonally or by mailing on or before the 12th day of July 1944, shall be deemed sufficient for the purpose of this application.

Dated: July 6th, 1944, New York City.

Edward A. Conger, United States District Judge.

[fol. 6] IN UNITED STATES DISTRICT COURT

[Same Title]

PETITION

Hon. Edward A. Conger, Judge of the United States District Court for the Southern District of New York:

The petition of Burton C. Meighan, Jr., as Substituted Trustee under the Last Will and Testament of William T. Wood, Deceased, respectfully shows:

I. That your petitioner resides at No. 21 Hazel Lane, Larchmont, Town of Mamaroneck, County of Westchester and State of New York.

II. That on the 17th day of March, 1930, one William T. Wood died a resident of the City, County and State of New York, leaving a Last Will and Testament dated the 18th day of August, 1925, and that said Last Will and Testament was duly admitted to probate in the Surrogate's Court of the County of New York on May 3rd, 1930. That in and by the terms and provisions of the said Last Will and Testament Larchmont National Bank and Trust Company and Burton C. Meighan, designated as executors and trustees in said will, duly qualified as such executors and trustees and entered upon their duties and continued to act as such until February 6th, 1933, when the said Burton C. Meighan died and that thereafter the Larchmont National Bank and Trust Company continued as surviving executor and trustee until August 5, 1933, when it was declared insolvent and put in the hands of a receiver; that thereafter, pursuant to [fol. 7] a judgment of the Supreme Court of the State of New York, County of Westchester, your petitioner was duly appointed substituted trustee under the said Last Will and Testament of William T. Wood, Deceased, and that your petitioner herein, pursuant to the said judgment, did duly qualify as said substituted trustee and is still qualified and continues to act as said substituted trustee as aforesaid.

III. That by an indenture of lease dated July 31, 1922, petitioner's predecessor in interest, Gramway Co. Inc., a New York corporation, leased to the debtor the land and building located at and known as 1553 Broadway, Borough of Manhattan, City, County and State of New York, for a term of twenty-one (21) years commencing May 1, 1926, to and including April 30, 1947, and thereafter, upon the terms and conditions therein set forth at the option of the debtor for a further term of twenty-one (21) years. By the said lease the debtor agreed to pay the landlord a net rental of Thirty thousand ($30,000.00) per year and, in addition, to pay taxes, insurance premiums and various other expenses of maintenance and operation.

IV. That paragraph 4 of the said lease provided:

"Conditional Limitation

4. The tenant covenants that if the rent reserved by this lease or any part thereof shall remain unpaid for more than ten days after written notice that it has become due or if the tenant shall fail to perform any of the covenants, conditions, provisions, and agreements herein contained, or, if a petition in bankruptcy shall be filed by the tenant or if the tenant shall be adjudged bankrupt or insolvent by any Court, or if a [fol. 8] trustee in bankruptcy of the tenant shall be appointed in any suit or proceeding brought by or against the tenant, then and in each and every such case, the term hereby granted shall immediately cease, determine and come to an end, and the landlord may recover and resume possession of the demised premises by any legal means."

A copy of the said lease and a copy of the agreement hereinafter mentioned by which the said lease was modified in certain respects will be submitted on the hearing of this application.

V. Thereafter the petitioner succeeded to all the rights and privileges of the Gramway Company, Inc., the aforesaid lessee, and that your petitioner became and still is the owner of the said premises located at and known as 1553 Broadway, New York City.

VI. That thereafter by an agreement between petitioner and the debtor, dated March 23, 1942, the aforesaid lease

was modified in certain respects, including a reduction of the rental upon conditions therein specified, which said agreement contained the following clause:

> "First. This agreement shall be of no force and effect and shall be null and void in any of the following events:
>
> "a) That a petition in bankruptcy or for reorganization under the Bankruptcy Laws of the United States shall be filed by the Tenant on or before April 30th, 1944;
>
> "b) That the Tenant make an assignment for the benefit of creditors or take advantage of any other insolvency statute or other statutes for the relief of debtors on or before April 30th, 1944;
>
> [fol. 9] "c) That should any petition in bankruptcy or for reorganization under the Bankruptcy Laws be filed against the Tenant on or before April 30th, 1944, the same shall not have been removed and any such proceeding dismissed or discontinued within thirty (30) days from the filing thereof;
>
> "d) That should a receiver or trustee for the Tenant's property be appointed, such receiver or trustee shall not have been removed in any proceeding connected therewith, dismissed or discontinued within thirty (30) days from the appointment of such receiver or trustee;
>
> and upon the occurrence of any of the foregoing events the Landlord shall be entitled to each and all of his rights as set forth in the Lease giving credit on his account, however, for all sums theretofore received."

VII. That on or about the 26th day of August, 1943, the debtor filed its petition herein for reorganization under Chapter X of the Bankruptcy Law. On the same date this Court appointed John F. X. Finn as trustee of the debtor. That thereupon the said trustee did enter upon and take possession of the aforesaid premises and has ever since remained and still remains in possession and control of the said premises and that the said trusteeship has not been vacated and the said bankruptcy proceedings have not been dismissed or discontinued.

VIII. That although petitioner has given due notice to the debtor and to the debtor's trustee of the cancellation and termination of the aforesaid lease pursuant to the terms thereof and has demanded possession of said premises, the said trustee refuses to surrender said possession and still remains in possession and control thereof.

[fol. 10] IX. That petitioner has leased the said premises to another tenant desiring immediate possession thereof and that substantial loss and damage will be suffered by petitioner by reason of his inability to give such possession unless the trustee and debtor forthwith surrender possession and control of said premises to petitioner.

X. That no other application has been made to this Court for the relief herein requested.

Wherefore petitioner prays that an order be made adjudging that the term granted by the aforesaid lease and all rights of the debtor and trustee therein have terminated and come to an end and that the debtor and its trustee be ordered forthwith to surrender possession of the said premises to petitioner and that a hearing be held upon this application upon such notice as the Court may direct and for such other and further relief in the premises as may be just and proper.

Dated: June 27, 1944.

Burton C. Meighan, Jr., As Substituted Trustee under the Last Will and Testament of William T. Wood, Deceased, Petitioner.

(Verified June 27, 1944.)

[fol. 11] In United States District Court

[Same Title]

Affidavit of Joseph Lorenz in Opposition to Petition

State of New York,
County of New York, ss:

Joseph Lorenz, being duly sworn, deposes and says:

I am a member of the firm of Lorenz, Finn & Lorenz, attorneys for the Trustee herein.

This affidavit is submitted in opposition to the petition of (a) The 415 Fifth Avenue Corporation, verified the 5th

day of July, 1944, and (b) the petition of Burton C. Meighan, Jr., Substituted Trustee under the Last Will and Testament of William T. Wood, Deceased, verified June 27, 1944. The petitioners are the respective owners of premises 1551 Broadway and 1553 Broadway, New York. They request that this Court adjudge that the terms of the leases of the Debtor upon the premises 1551 and 1553 Broadway, New York, and all rights of the Debtor and Trustee therein, have terminated and that the Trustee be ordered to surrender said premises to the petitioners.

The Debtor, and since his appointment, the Trustee, have operated a restaurant on these contiguous properties.

The premises at 1551 Broadway were leased by the Debtor by an Indenture of Lease dated May 19, 1931, at a net rental of $49,000 per year, plus taxes, insurance premiums, and other similar items. The expiration date was May 1, 1947. Paragraph 2 of said lease contained the following provision:

> "If during the term hereby demised the Lessee file a petition in bankruptcy or be adjudicated a bankrupt [fol. 12] or make a general assignment or take the benefit of any insolvent act, or if a Receiver or Trustee be appointed for the Lessee's property, and such Receivership or Trusteeship shall not be vacated within thirty (30) days after the appointment of such officers, then in any of those events the Lessor may at its option cancel and terminate this Lease and upon the exercising of such option this Lease shall thereupon come to an end and be of no further force or effect and shall not pass by operation of law, and the Lessor shall have the right immediately to take possession by force or otherwise or institute any proceedings for the purpose of obtaining such possession."

This lease was modified by an agreement between The 415 Fifth Avenue Corporation and the Debtor dated May 1, 1941. The modification agreement, in paragraph First thereof, contained a provision that it should be null and void if "a petition in bankruptcy or for reorganization under the Bankruptcy Laws of the United States shall be filed by the lessee on or before April 30, 1944." It also provided that the minimum rental payable under the original lease should be reduced for the period from May 1,

1941 to May 1, 1947 to $36,000 per annum, plus taxes, insurance premiums and similar items, and also a sum equal to 6.2025% of the amount by which gross sales in the demised premises during each of said years should exceed the sum of $564,280.

The modification agreement with respect to 1551 Broadway, also provided that the expiration date of the lease be extended from May 1, 1947 to May 1, 1957, subject, however, to the following terms and conditions: at any time prior to February 1, 1946, the lessor might give notice to the lessee that it cancelled and revoked the ex- [fol. 13] tended term beyond May 1, 1947; the minimum annual for the extended period (exclusive of percentage rent and taxes and insurance payments) should be at least $35,000; that said annual minimum rent for the extended period should be equal to at least 6% of the value of the premises as of February 1, 1946, but not less than $35,000 per annum; that if the parties were unable to agree upon the minimum rent as represented by 6% of the value of said premises, it was to be determined by appraisers appointed by the parties; that despite the decision of said appraisers, the lessor, nevertheless, had the right on or before August 1, 1946, if it did not like the appraisers' determination, to cancel, and to refuse to extend the term beyond May 1, 1947.

The lease of the premises 1553 Broadway, dated July 31, 1922, provided that it was to expire on April 30, 1947, at a net rental to the landlord of $30,000 per annum and taxes, insurance premiums and similar items. It contained a provision in paragraph 4 thereof as follows:

> "The tenant covenants that if the rent reserved by this lease or any part thereof shall remain unpaid for more than ten days after written notice that it has become due or if the tenant shall fail to perform any of the covenants, conditions, provisions, and agreements herein contained, or if a petition in bankrupty shall be filed by the tenant or if the tenant shall be adjudged bankrupt or insolvent by any Court, or if a trustee in bankruptcy of the tenant shall be appointed in any suit or proceeding brought by or against the tenant, then and in each and every such case, the term hereby granted shall immediately cease, determine and come to an end, and the landlord may recover and resume

possession of the demised premises by any legal means."

[fol. 14] This lease was modified by an agreement between the landlord and the Debtor, dated March 23, 1942, whereby the annual fixed rent was reduced to $22,041.11 per annum until April 30, 1947, plus a percentage rent of 3.7975% of the amount by which gross sales in the demised premises should exceed the sum of $564,280. The modification agreement contained a clause to the effect that:

"First: This agreement shall be of no force and effect and shall be null and void in any of the following events: (a) That a petition in bankruptcy or for reorganization under the Bankruptcy Laws of the United States shall be filed by the Tenant on or before April 30, 1944 * * *"

Said modification agreement also provided for an extension of the lease to May 1, 1957, subject, however, to the following provisions: that any time prior to February 1, 1946, the landlord might give notice to the tenant that he cancelled and revoked the extended term beyond April 30, 1947; that the minimum rent (exclusive of percentage rent, taxes and insurance, etc.) for the extended period should be a sum equal to 6% of the value of the demised premises, but in no event less than the annual rent abovementioned; that if the parties could not agree upon such minimum rent, it was to be determined by appraisers; that such appraisal was to be binding upon the parties (but not less than the abovementioned sum), but with the same extraordinary provision as appears in the modification agreement covering 1551 Broadway that the landlord nevertheless had the right at any time on or before August 1, 1946, notwithstanding such appraisal, to notify the tenant that there should be no extension of the lease and that it should finally cease and terminate on April 30, 1947.

As the leases with respect to 1551 Broadway and 1553 Broadway are entirely separate, and each landlord has the [fol. 15] right to act independently of the other, it is possible under these provisions of the modification agreements, that one of said landlords should exercise the right to cancel the extension of his lease so as to terminate it in 1947, while the other landlord might not cancel the extension in his lease. Accordingly, although the premises

have been and are operated as a single unit, the Debtor might be left with only one of the two parcels.

Shortly after the appointment of the Trustee, numerous conferences were had by the Trustee, the officers of the Debtor, your deponent and other interested parties, with respect to the policy to be pursued in connection with the leases covering the combined premises. At the Trustee's request, a comprehensive analysis of the operations of the Debtor in said premises over a ten year period was prepared. This analysis disclosed, in the opinion of the Trustee and the officers of the Debtor, that the combined rent paid for the premises was excessive from the point of view of a long term lease not expiring until 1957. The rent, even under the modified leases, taking into consideration the taxes and insurance payable by the Debtor, and after deducting all net income received from the buildings, other than the restaurant, amounts to almost $73,000 per annum.

On the basis of the average sales of the restaurant during the period 1934-1942 inclusive, this rent of $73,000 represented in excess of 19% of total sales. Even on the basis of sales for the year August 1, 1942 to July 31, 1943, the percentage of the rent to the total sales was close to 14%. Although operations for the years 1942 and 1943, and current operations are highly profitable, in the year 1938, the Debtor suffered a loss of $10,727 in the operation of the premises; in 1939, a profit of $406 was made; in 1940, a loss of $11,493 was incurred; in 1941 a profit of $12,319 was made. Thereafter, largely as a result of un- [fol. 16] usual conditions in the Times Square area, the profits have greatly increased.

It should be noted further that during the period from 1934 to 1943 inclusive, labor costs, which constitute a large portion of restaurant operating costs, almost doubled in amount. A considerable part, moreover, of the profits from the operation of the restaurant arises from liquor sales, which have had a pronounced increase in volume during the last two years. As is well known, there was a serious question in the latter part of 1943 and the early part of 1944 as to whether liquor would be available in sufficient quantities to meet requirements. This constituted another hazard in connection with assumption of the modified lease for the full term upon the terms thereof.

After various discussions between the Trustee, the Debtor's officers, the Trustee's counsel, and other interested parties, it was decided to endeavor to obtain a reasonable modification in the terms of said leases; and deponent was instructed by the Trustee to proceed with such negotiations.

Accordingly, on December 6, 1943, deponent had a conference with Messrs. Lowell Birrell and Herbert Birrell, representing the owners of 1551 Broadway. Although these gentlemen stated that they did not represent the owner of the premises at 1553 Broadway, deponent was advised that the respective owners were cooperating with respect to their properties and that the owner of 1553 Broadway would be kept informed as to the views expressed. At this meeting deponent, on behalf of the Trustee, requested a reasonable reduction in rent, emphasizing particularly the high ratio of fixed rent to sales, the greatly increased labor costs, and the probable lack of permanence in the then current operating results in the light of the record in the restaurant over a long term period and during normal times. Mr. Lowell Birrell stated that he would take the matter up with the interested parties and would advise deponent of their views.

[fol. 17] Deponent heard nothing from Mr. Birrell until January 27, 1944, when Mr. Lowell Birrell telephoned deponent and stated that a meeting of the Board of Directors of the owner of 1551 Broadway had been held, and that said Board of Directors desired to know forthwith whether the Trustee would assume the lease of the premises upon the terms specified in the modified lease. A conference was arranged for the following day at which the matter was to be discussed. In the meantime, deponent conferred with respect to the situation with the Trustee, the officers of the Debtor, representatives of the Securities and Exchange Commission, and others interested. The Trustee also obtained an appraisal of the leasehold by Mr. Francis K. Stevens of Brown, Wheelock, Harris, Stevens, Inc. Mr. Stevens appraised the fair net rental value of the entire property—namely, the two leaseholds—at $35,000 net per annum, as against the sum of approximately $58,000 net rental, payable under the modified leases (exclusive of taxes, etc.). All parties with whom deponent discussed the matter agreed that, if possible, a modification of the leases should be effected whereby the fixed minimum

rent should be reduced to a reasonable level from the point of view of a long term lease, but that the landlords should be offered, in addition to the fixed minimum rent, an advantageous "percentage rental" based on sales so that in periods when the business of the Debtor justified it, the landlords would receive at least as much and probably more than they were then receiving, but in periods of recession, the Debtor would be protected by being required to pay only a reasonable fixed minimum.

On the following day, January 28, 1944, Mr. Herbert Birrell, a partner of Mr. Lowell Birrell, came to the appointed conference, stating that his brother had been called to Washington and would not be able to attend. There was also present Mr. Kenneth LaBarre, a Vice President of the Debtor. Mr. Birrell asked whether the [fol. 18] Trustee would advance a sufficient sum to pay taxes accrued against the respective premises. To this deponent readily consented, and such advances were shortly thereafter made. The parties at the meeting thereupon proceeded to discuss the subject matter for which the meeting had been arranged—the request of the landlord as transmitted to the deponent for immediate decision as to whether the Trustee would assume the leases.

Deponent thereupon stated that, in his opinion, a satisfactory solution of the problem would be to reduce the fixed minimum provided for in the leases and to supplement the same by a favorable percentage rental which would net the landlords in prosperous times even more than they were entitled to receive under the modified leases, but that the tenant would be protected by the obligation to pay only a reasonable minimum rental during less favorable periods. Mr. Birrell stated that he thought the suggestion was a good one, that personally he favored leases of such a character, but that, of course, he was not authorized to accept such a proposal without taking it up with his principals. He stated, however, that he would take the matter up with his principals and would shortly advise deponent. Deponent promptly informed the Trustee, the Debtor's officers, and representatives of the Securities and Exchange Commission of this proposal made to Mr. Birrell and his comments and reaction thereon.

Thereafter, on January 31, 1944, February 2, 1944, and February 7, 1944 deponent had discussions on the telephone with Mr. Herbert Birrell with respect to payments

on account in connection with use and occupation. At one of these discussions, deponent asked Mr. Birrell what the attitude of his client was with respect to the proposal made at the conference on January 28th; and requested a further conference at which, if possible, an [fol. 19] agreement could be consummated. Mr. Birrell said that it was not possible to arrange a meeting at that time as his brother Lowell Birrell, was in, or was going to go to Chicago, and would be away for approximately ten days; he stated further that the question of whether or not a lease in which the payment of percentage rent played an important part, would be acceptable, would depend in large part on what the management of the Childs Company would be upon reorganization; and as some time would necessarily elapse before reorganization could be effected, he thought it would be preferable to wait until the reorganization was further along before coming to a decision. He stated further that by virtue of these facts there was no necessity of any hurry in coming to a conclusion. He stated, further, that he would subsequently communicate with deponent with respect to this matter.

No further word was received from either of the landlords or their attorneys until March 20, 1944 when Mr. Lowell Birrell telephoned deponent threatening to cancel the lease on 1551 Broadway. A conference was arranged for March 23, 1944, at which there were present Mr. Lowell Birrell, Mr. Herbert Birrell, Mr. LaBarre and deponent. Mr. Birrell threatened cancellation of the lease and asked whether the Trustee would give up the premises. Deponent stated that in his opinion the Trustee would not surrender the premises in view of the current favorable operating results, and stated further that in his opinion, the respective landlords had waived any right they might have to cancel their leases by virtue of the long period of time which had elapsed since the appointment of the Trustee. Deponent also mentioned the conversation he had had with Mr. Herbert Birrell on January 28, 1944 with respect to a lease with a liberal percentage clause, and the subsequent telephone conversations with him as above related.

Notwithstanding that deponent had expressed the view at the conference on March 23, 1944 that the lapse of time [fol. 20] had constituted a waiver on the part of the landlords of any right they might have to cancel the leases,

no communication was received from either of the landlords or their attorneys with respect to any proposed cancellation for approximately three months, as hereinafter set forth. Accordingly, on May 9, 1944, deponent wrote Mr. Birrell as follows:

> "The Trustee of Childs Company is desirous of assuming the lease at 1551 Broadway, as modified. I trust that this is satisfactory to your client and I would appreciate it, if at your convenience, you would communicate with me in connection with the details to consummate the assumption."

On the same date, a similar letter was written by deponent to the attorneys for 1553 Broadway.

No reply was ever received to either of said letters. Accordingly, on May 31, 1944, the Trustee caused to be sent to the respective lessors checks which, added to the payments for use and occupation theretofore made to them, aggregated the full rent payable to said landlords under their modified leases. These checks were returned by the respective landlords. Still, however, no action was taken by the landlords or notices given of any proposed cancellation until June 23, 1944, when the owner of the premises 1553 Broadway served a written notice upon the Trustee and the Debtor stating that the lease of said premises as modified "has ceased, determined and come to an end by virtue of the bankruptcy proceedings now pending in the United States District Court, Southern District of New York, relating to the said Childs Company * * *", and also demanding that the Trustee and the Debtor vacate said premises. On the same date, a notice was served by the landlord of the premises 1551 Broaway stating that it cancels and terminates the lease with the Childs Company covering said premises, and that agree-
[fol. 21] ment of modification of said lease is null and void. Said notice stated further that "pursuant to provisions of paragraph 2 of said Indenture of Lease dated May 19, 1931, (the landlord) hereby exercises its option to cancel and terminate the lease."

Thereafter the present proceedings were instituted by the respective landlords.

Deponent is unaware when negotiations were commenced by the landlords with the new lessee mentioned in the

respective petitions, but believes that such negotiations were pending at the time of the aforesaid discussions with Mr. Herbert Birrell with respect to the proposed modification of the Debtor's leases so as to provide for a reduced fixed rental and an increased percentage rent. No notice of cancellation was sent by either landlord until June 23, 1944, despite the fact that they knew that deponent contended, as early as March 23, 1944, that any right of the lessors to cancel the respective leases had already been waived by them. Deponent believes that the continued delay was for the sole purpose of enabling the landlords to consummate their new proposed lease while still having the advantage of the Childs Company occupancy of the premises.

Deponent, therefore, submits (a) that the appointment of the Trustee in the present reorganization proceedings is not a ground for cancellation of the lease covering 1553 Broadway, under the terms of said lease; (b) that if such appointment of the Trustee were construed to be a ground for cancellation under said lease, the landlord of said premises has waived his right and is estopped to do so; and (c) that the landlord of premises 1551 Broadway has waived its right to exercise and is estopped from exercising any option to cancel its lease.

Deponent accordingly prays on behalf of the Trustee, that the respective petitions of the landlords of 1551 Broadway and 1553 Broadway be denied.

Joseph Lorenz.

(Sworn to July 24, 1944.)

[fol. 22] IN UNITED STATES DISTRICT COURT

[Same Title]

AFFIDAVIT OF JOHN F. X. FINN IN OPPOSITION TO PETITION

STATE OF NEW YORK,
County of New York, ss:

JOHN F. X. FINN, being duly sworn, deposes and says:

I am the Trustee of the Debtor herein, having been appointed by order of this Court dated August 26, 1943.

I have read the affidavit of Joseph Lorenz, sworn to

July 24, 1944, in opposition to the respective petitions of the owners of premises 1551 Broadway and 1553 Broadway, New York, requesting an adjudication by this Court that the leases covering said premises be terminated and cancelled, and requesting further that deponent be ordered to vacate said premises.

Although, as set forth in the affidavit of Mr. Lorenz, the rent of said respective premises as provided in the modified leases covering them, is excessive from the point of view of a long term lease, and, although, upon assumption, a substantial reserve should be set up out of the present earnings, as a safeguard against possible operating losses in the future, nevertheless, deponent believes that it is to the advantage of the Debtor's estate to assume said leases, as modified, in view of the high current operating profits of the restaurant maintained at that location. It is to be noted, moreover, that the Debtor has a substantial unamortized investment in said premises as of December 31, 1943, of $68,562.

In view of the above facts and those set forth in said affidavit of Mr. Lorenz, deponent respectfully requests that said petitions be denied.

John F. X. Finn.

(Sworn to July 24, 1944.)

[fol. 23] In United States District Court

[Same Title]

Affidavit of Kenneth LaBarre in Opposition to Petition

State of New York,
County of New York, ss:

Kenneth LaBarre, being duly sworn, deposes and says:

I am a Vice President of Childs Company, the Debtor herein.

I have read the affidavit of Joseph Lorenz, sworn to July 24, 1944, in opposition to the petitions of the landlords of the respective premises 1551 Broadway and 1553 Broadway, New York, requesting an adjudication that said leases have been cancelled and terminated, and that the

Trustee herein be ordered to surrender said premises to the petitioners.

I was present at the conference at the office of Mr. Joseph Lorenz held on January 28, 1944, at which there were present Mr. Herbert Birrell, Mr. Lorenz, and deponent. I was also present at the conference at Mr. Lorenz' office held on March 23, 1944, as set forth in his affidavit. At this conference there were present Mr. Lowell Birrell, Mr. Herbert Birrell, Mr. Lorenz and deponent.

Said affidavit of Mr. Lorenz correctly sets forth what transpired at these two conferences.

Kenneth LaBarre.

(Sworn to July 24, 1944.)

[fol. 24] IN UNITED STATES DISTRICT COURT

[Same Title]

ORDER OF REFERENCE IN RE PREMISES 1551-1553 BROADWAY, NEW YORK, N. Y.

The petition of Burton C. Meighan, Jr., Substituted Trustee under the Last Will and Testament of William T. Wood, Deceased, verified June 27, 1944, praying for an order (1) Adjudging that the term granted by a certain indenture of lease dated July 31, 1922, made by and between Gramway Company, Inc., as landlord, and Childs Company, as tenant, and as modified in certain respects by an agreement dated the 23rd day of March, 1942, made by and between Burton C. Meighan, Jr., as Substituted Trustee under the Last Will and Testament of William T. Wood, Deceased (the successor of all the rights and privileges of the Gramway Company, Inc.), as landlord, and Childs Company, as tenant, has terminated and come to an end; and (2) Authorizing and directing John F. X. Finn, as trustee of the debtor herein, and the said debtor to forthwith surrender possession of premises located at and known as 1553 Broadway, Borough of Manhattan, City, County and State of New York, to said Burton C. Meighan, Jr., as Substituted Trustee as aforesaid; and the petition of The 415 Fifth Avenue Corporation, verified July 5, 1944, praying, *inter alia*, for an order adjudging that all rights of the Childs Company and of John F. X.

Finn, Trustee of the Debtor, under an indenture of lease dated May 19, 1931, between the 1551 Broadway Corporation and the Debtor, as modified by agreement dated May 1, 1941, have been terminated, and further that the [fol. 25] Trustee of the Debtor be ordered forthwith to surrender said premises to petitioner, The 415 Fifth Avenue Corporation, having duly come on to be heard on the 25th day of July, 1944, and due notice of said applications having been given as prescribed by this Court in its Orders dated July 6, 1944, and after hearing Meighan & Necarsulmer, Esqs., attorneys for Burton C. Meighan, Jr., as Substituted Trustee, etc., and Birrell & Birrell, Esqs., attorneys for The 415 Fifth Avenue Corporation, in support of the aforesaid applications, and Lorenz, Finn & Lorenz, Esqs., attorneys for the Trustee herein, in opposition thereto, and due deliberation having been had thereon;

Now, upon the petition of Burton C. Meighan, Jr., as Substituted Trustee, etc. and The 415 Fifth Avenue Corporation, the answering affidavit of Joseph Lorenz, sworn to July 24, 1944, the affidavit of John F. X. Finn, as Trustee, sworn to July 24, 1944, the affidavit of Kenneth LaBarre, sworn to July 24, 1944, the reply affidavit of Herbert A. Birrell, sworn to July 25, 1944, and upon all the proceedings heretofore had herein, it is

Ordered, that the issues raised by the petition of Burton C. Meighan, Jr. and the petition of The 415 Fifth Avenue Corporation, the answering affidavit of Joseph Lorenz, sworn to July 24, 1944, the affidavit of John F. X. Finn, as Trustee, sworn to July 24, 1944, the affidavit of Kenneth LaBarre, sworn to July 24, 1944, the reply affidavit of Herbert A. Birrell, sworn to July 25, 1944, be, and the same hereby are, referred to Hon. Robert P. Stephenson as Special Master to hear the proofs and arguments of the parties and report his findings of fact and conclusions of law thereon to this Court with all convenient speed; and it is further

[fol. 26] Ordered, that any party in interest herein be, and he hereby is, granted permission to file appropriate answers with the aforesaid Special Master.

Dated, July 26th, 1944.

Edward A. Conger, U. S. D. J.

[On the hearing before Hon. Robert P. Stephenson, Special Master, the following Answer of Appellant was required to be filed by the said Special Master in connection with said hearing in place of the preceding affidavits.]

[fol. 27] IN UNITED STATES DISTRICT COURT

[Same Title]

ANSWER

John F. X. Finn, as Trustee of Childs Company, Debtor, (hereinafter called the Trustee), answering the petition of Burton C. Meighan, Jr., as Substituted Trustee under the Last Will and Testament of William T. Woods, Deceased, alleges as follows:

1. The Trustee has no knowledge or information sufficient to form a belief as to any of the allegations set forth in paragraphs I and II of the petition.

2. Admits the allegations set forth in paragraphs III, IV and V of the petition.

3. Denies each and every allegation set forth in paragraph VI of the petition, except admits that an agreement was entered into between the petitioner and the Debtor, dated March 23, 1942, modifying the lease mentioned in the petition in certain respects, including the reduction of the rental; admits that said agreement of March 23, 1942 contains the provisions set forth in paragraph VI of the petition; and denies the legality or validity of (a) any provisions in said agreement purporting to render null and void the reduction of rental provided in said agreement of March 23, 1942, in the event that a Petition for Reorganization under the Bankruptcy Laws of the United States should be filed by the tenant on or before April 30, 1944, and (b) the provision in said agreement that in such event the peti- [fol. 28] tioner would be entitled to all his rights under the original lease giving credit only for all sums theretofore received.

4. Admits the allegations set forth in paragraph VII of the petition.

5. Denies each and every allegation set forth in paragraph VIII of the petition, except admits that petitioners on or about June 23, 1944, served a notice upon the Debtor and the Trustee, wherein petitioner purported to notify the Debtor and Trustee of the cancellation and termination of the lease and demanded possession of said premises, and admits that the Trustee refuses to surrender said possession and still remains in possession and control thereof.

6. Denies any knowledge or information sufficient to form a belief as to any of the allegations set forth in paragraph IX of the petition.

And for an affirmative defense, the trustee alleges as follows:

7. At various times since the early part of December, 1943, the Trustee, through his attorneys, has been negotiating with the owners and landlords of the respective premises at 1551 Broadway and 1553 Broadway, New York, with respect to the terms of the respective leases covering said premises. The attorneys for the owner of the premises at 1551 Broadway are Messrs. Birrell & Birrell. The attorneys for the owner of the premises at 1553 Broadway are Messrs. Meighan & Necarsulmer. The negotiations were at all times actually conducted with Messrs. Birrell & Birrell. The Trustee and his attorneys at all times understood that Messrs. Birrell & Birrell were not representing the owner [fol. 29] of premises 1553 Broadway as attorneys, but the Trustee (through his attorneys) was advised by Messrs. Birrell & Birrell in the early part of said negotiations that the respective owners of 1551 Broadway and 1553 Broadway were acting and intended to act in common as their respective premises were utilized as a single restaurant by the Debtor and the Trustee; that the owner of 1553 Broadway relied upon the real estate knowledge, experience, and judgment of the officers and directors of the corporate owner of 1551 Broadway; and that the petitioner herein and his attorneys were being advised of the negotiations occurring from time to time between the attorneys for the owner of 1551 Broadway and Trustee's attorneys. On information and belief, the petitioner and his attorneys were in fact currently advised from time to time of all the negotiations between the Trustee's attorneys and the attorneys for the

owner of the premises at 1551 Broadway, and approved the same.

8. On or about January 27, 1944, Messrs. Birrell & Birrell advised the Trustee, through the latter's attorney, that the owners of 1551 Broadway desired an immediate decision by the Trustee as to whether the Trustee would assume the leases, as modified, of the premises at 1551 Broadway and 1553 Broadway. Thereupon a conference was arranged on January 28, 1944 at which the matter was to be discussed. At said conference, the Trustee by his attorney advised Mr. Herbert Birrell of the above-mentioned firm, that, if possible, the Trustee should like to have the leases on said respective premises modified so as to provide for a reasonable reduction in the fixed minimum rent and an increase in the additional rent payable to the lessors, to be represented by a larger percentage of the gross sales at the restaurant operated on the said premises, the effect of which would be to afford the landlords current rent at least as large and [fol. 30] probably larger than they were then entitled to receive under the existing leases as modified, yet would protect the tenant against unreasonably high rentals at times when business conditions were less favorable. Mr. Herbert Birrell at that time advised the Trustee's attorney in effect that he personally favored such a proposal, but he would be obliged to discuss the matter with his principals before an answer could be given. Within a week thereafter, the Trustee's attorney asked Mr. Herbert Birrell what the attitude of the lessors was with respect to said proposal. The Trustee's attorney was then advised that the attitude of the landlords of the premises toward said proposal would depend largely upon who would constitute the management of the Debtor upon its reorganization, that this was a vital aspect of any lease in which a percentage of gross sales constituted an important element of rent, that as it would necessarily take some time before the reorganization of the Debtor could be effected, the lessors would consider the proposal when the proceedings for reorganization had progressed further, that, therefore, there was no hurry in the matter, and that Mr. Herbert Birrell or his brother, Mr. Lowell Birrell, would subsequently get in touch with the Trustee's attorney in such connection. On information and belief, the petitioner was advised of said proposals and discussions.

9. On information and belief, petitioner intended that the Trustee should rely upon said statements; the Trustee in

fact did rely thereon, and, in consequence, did not at that time offer or take steps to assume said leases.

10. On information and belief, that in fact the petitioner, at the respective times said statements were made to the Trustee's attorney, intended to cancel his said lease and to enter into a new lease with other parties; that he had no [fol. 31] intention of entering into an agreement with the Trustee upon the basis of the above mentioned discussions or upon substantially such basis.

11. On information and belief, petitioner at the time of said conference and discussions with the Trustee's attorney, was negotiating a lease said premises to other parties, and desired that the Trustee should not either seek to assume or reject said lease or take action to that end until after petitioner's negotiations with the new proposed lessee should be consummated; and said statements were made to Trustee's attorney with the intent and purpose of inducing and causing the Trustee to take no such action until after the conclusion of petitioner's said negotiations with other parties.

12. On or about March 23, 1944, Trustee's attorney on his behalf advised Messrs. Lowell Birrel and Herbert Birrell that, in his opinion, the respective landlords of the premises at 1551 Broadway and 1553 Broadway had waived their right, if any, to cancel the leases upon said properties by virtue of the long period of time which had elapsed since the appointment of the Trustee without action on their part to cancel said leases. Nevertheless, and despite the further fact that the Trustee was appointed on August 26, 1943, no notice of cancellation or other notice purporting to cancel said lease of the premises at 1553 Broadway was given by petitioner until on or about June 23, 1944.

13. By virtue of the above facts, the petitioner has waived its right to exercise any option to cancel said lease and is estopped from so doing.

[fol. 32] Wherefore the Trustee requests that the petition herein be denied and dismissed.

John F. X. Finn, As Trustee of Childs Company, Debtor.

(Verified July 28, 1944.)

[By agreement among the parties hereto the testimony is omitted from the printed record.]

[fol. 33] PETITIONER-APPELLEE'S EXHIBIT 1

[Only pertinent portions of this Exhibit are printed herein pursuant to agreement with counsel.]

"Agreement made this 31st day of July, 1922 between Gramway Company, Inc., a domestic corporation having its principal place of business at 54 West Boston Post Road, in the Town of Mamaroneck, County of Westchester and State of New York, hereinafter referred to as "landlord" and Childs Company a domestic corporation having its principal place of business at No. 200 Fifth Avenue, Borough of Manhattan, City, County and State of New York, hereinafter referred to as "tenant," Witnesseth:

* * * * * * *

"Conditional Limitation

"4. The tenant covenants that if the rent reserved by this lease or any part thereof shall remain unpaid for more than ten days after written notice that it has become due or if the tenant shall fail to perform any of the covenants, conditions, provisions, and agreements herein contained, or, if a petition in bankruptcy shall be filed by the tenant or if the tenant shall be adjudged bankrupt or insolvent by any Court, or if a trustee in bankruptcy of the tenant shall be appointed in any suit or proceeding brought by or against the tenant, then and in each and every such case, the term hereby granted shall immediately cease, determine and come to an end, and the landlord may recover and resume possession of the demised premises by any legal means.

* * * * * * *

[fol. 34] "Recovery of Possession on Default

13. The tenant covenants that if the rent reserved by this lease, or any part thereof, shall remain unpaid for more than ten days after written notice that same has become due, or the tenant shall fail to perform any covenant, condition, provision or agreement herein contained or if a petition in bankruptcy shall be filed by the tenant or if the tenant shall be adjudged insolvent by any Court, or if a trustee in bankruptcy of the tenant, shall be appointed in any suit or proceeding by or against the tenant, or if the tenant

shall be dispossessed or if the demised premises shall become vacant or abandoned, the landlord may recover and resume possession of the demised premises by force or otherwise, without being liable to prosecution therefor. . . .

. . . . . .

[fol. 35] PETITIONER-APPELLEE'S EXHIBIT 3

To John F. X. Finn, As Trustee in Bankruptcy of Childs Company; c/ Lorenz, Finn & Lorenz, Esqs., Attorneys for Trustee, 165 Broadway, New York, N. Y.; Childs Company, 200 Fifth Avenue, New York, N. Y.

Please take notice that the term granted under and by virtue of a certain written lease dated July 31, 1922, made by Gramway Company Inc., as landlord, and Childs Company, as tenant, covering the premises known as 1553 Broadway, Borough of Manhattan, City, County and State of New York, and as modified in certain respects by an agreement dated March 23, 1942, has ceased, determined and come to an end by virtue of the bankruptcy proceedings now pending in the United States District Court, Southern District of New York, relating to the said Childs Company, the aforesaid tenant.

Please take further notice that Burton C. Meighan, Jr., as Substituted Trustee under the Last Will and Testament of William T. Wood, Deceased, as owner in fee of the said premises known as 1553 Broadway, New York City, and as successor to all of the rights and privileges of the said Gramway Company Inc. under and by virtue of the aforesaid lease, does hereby demand that you vacate the said premises at 1553 Broadway, New York City, and deliver possession thereof to the said Burton C. Meighan, Jr., as Substituted Trustee as aforesaid, forthwith.

[fol. 36] Please take further notice that the said Burton C. Meighan, Jr., as Substituted Trustee, as aforesaid, has leased the entire premises at 1553 Broadway, New York City, to a tenant desiring immediate possession of the said premises. In the event of your failure to comply with this demand resulting in loss or damage of any nature whatsoever to the said Burton C. Meighan, Jr., as Substituted

Trustee as aforesaid, proceedings will be instituted to recover for any and all said loss or damage.

Dated June 23, 1944.

Burton C. Meighan, Jr., As Substituted Trustee under the Last Will and Testament of William T. Wood, Deceased, Landlord.

[fol. 37] PETITIONER-APPELLEE'S EXHIBIT 4

Letterhead of

Meighan & Necarsulmer

Counselors at Law

120 Broadway

New York 5, N. Y.

June 1, 1944.

Mr. John F. X. Finn, As Trustee of The Childs Company, 165 Broadway, New York City, N. Y.

DEAR MR. FINN:

Re: William T. Wood Estate (Premises #1553 Broadway)

I have had before me for some time a letter from Mr. Joseph Lorenz indicating that you are desirous of assuming the lease of #1553 Broadway as modified by agreement dated March 23, 1942. This letter has been given careful consideration. In view of the bankruptcy the modified lease above referred to is no longer in effect.

As you know, I am under certain statutory disabilities as a testamentary trustee and in any event in connection with any new lease-relationship would be required to proceed under the applicable sections of the Real Property Law.

Furthermore, an investigation has convinced me that the fair rental value of the property is in excess of the net rental of $22,041.11.

I am this day in receipt of a letter signed in your name by Mr. LaBarre, Vice President of the Childs Company, [fol. 38] enclosing a check to my order in the sum of $10,-

775.08, together with a statement which purports to bring to date the obligations of the tenant under the modification agreement. In view of the circumstances above outlined I cannot retain the check and am therefore returning it to you herewith.

As a matter of courtesy, a copy of this letter is being sent to the Childs Company at its executive offices for the attention of Mr. LaBarre.

Faithfully yours, Burton C. Meighan, Jr.

enclosure.

PETITIONER-APPELLEE'S EXHIBIT 5

Letterhead of

Lorenz, Finn & Lorenz

165 Broadway

New York

July 6, 1944.

Barton C. Meighan, Jr., Messrs. Meighan & Necarsulmer, 120 Broadway, New York 5, N. Y.

DEAR MR. MEIGHAN:

Enclosed is a copy of letter which I have written Mr. Herbert Birrell, which is self-explanatory.

Very truly yours, Joseph Lorenz.

JL m.

[fol. 39] Letterhead of Lorenz, Finn & Lorenz, 165 Broadway, New York

July 6, 1944.

Re: 1551 Broadway, 1553 Broadway

Herbert A. Birrell, Esq., 545 Fifth Avenue, New York 17, N. Y.

DEAR MR. BIRRELL:

I acknowledge receipt of your letter of July 5th.

I do not believe that either you or your brother gave me any reason to misunderstand your relationship to the William W. Wood Estate or to its attorneys, nor did I

misunderstand it. I have at all times known that you do not legally represent the William T. Wood Estate, but that said estate is represented by Messrs. Meighan and Necarsulmer. It has been my understanding that the two landlords were naturally cooperating, and, I assumed that your firm, without committing the Wood Estate in any way, was expressing the joint views of the two landlords on the matters we have been discussing. I did, in fact, as I expressed to Mr. Meighan, have some hesitation in telephoning or calling him about the subject matter of our discussions in view of the fact that we had been talking only with your firm, and I did not wish to imply, by directly communicating with Mr. Meighan, that I had any doubt that you were accurately expressing his view point.

I repeat that no misunderstanding has existed on my part, nor do I believe that any harm whatsoever has been done, nor anyone's rights prejudiced. I am sending a copy of this letter to Mr. Meighan.

Very truly yours, sgd. Joseph Lorenz.

JL/m

[fol. 40] RESPONDENT'S-APPELLANT'S EXHIBIT "D"

Letterhead of Lorenz, Finn & Lorenz, 165 Broadway New York

May 9, 1944,

Re: Childs Company 1553 Broadway

Burton C. Meighan, Jr., c/o Messrs. Meighan & Necarsulmer, 120 Broadway, New York 5, N. Y.

DEAR MR. MEIGHAN:

The Trustee of Childs Company is desirous of assuming the lease at 1553 Broadway, as modified. I trust that this is satisfactory to your client and I would appreciate it, if at your convenience, you would communicate with me in connection with the details to consummate the assumption.

Very truly yours, Joseph Lorenz.

JL/m

[fol. 41]. In United States District Court

[Same Title]

Report of Special Master on Petition of Burton C. Meighan, Jr., Substituted Trustee Under the Last Will and Testament of William T. Wood, Deceased

To the Honorable Judges of the United States District Court for the Southern District of New York:

Robert P. Stephenson, duly appointed Special Master herein by order dated July 26, 1944, heard the evidence on the issues presented by the petition of Burton C. Meighan, Jr., Substituted Trustee under the Last Will and Testament of William T. Wood, Deceased, verified June 27, 1944 and the answer thereto by John F. X. Finn, trustee of the above named debtor verified July 28, 1944 and the arguments of counsel on August 3 and 4, 1944, and after due deliberation and the rendering of an opinion dated August 7, 1944 hereto annexed, respectfully reports as follows:

Findings of Fact

1. On July 31, 1922 the petitioner's predecessor in interest made a lease with Childs Company, which is in evidence and marked Petitioner's Exhibit 1.

2. The petitioner is the substituted trustee under the last will and testament of William T. Wood, deceased, and is the successor in interest to the landlord in said [fol. 42] lease, to the reversion of said lease, and all the rights of the original lessor therein.

3. On May 23, 1942, the petitioner and Childs Company entered into a modification which is in evidence and marked Petitioner's Exhibit 2.

4. On August 26, 1943, Childs Company, the debtor herein, filed its petition for reorganization under Chapter X of the Bankruptcy Act, and in such petition stated that it is unable to pay its debts as they mature.

5. On August 26, 1943, the judge entered an order approving said petition.

6. On August 26, 1943, John F. X. Finn was appointed trustee of the debtor in said proceeding. He took pos-

session and now has possession of the premises covered by the aforesaid lease and has been paying to the petitioner from time to time sums on account of use and occupation with the stipulation that none of such payments should affect the rights or liabilities of either party.

7. From about December 6, 1943 until shortly after January 28, 1944, the trustee through his attorney was negotiating with the attorneys for an adjoining landlord, whose name is The 415 Fifth Avenue Corporation. The discussion in these negotiations covered the making of new leases. The attorneys for The 415 Fifth Avenue Corporation had at times suggested that their client might make a lease with the trustee with substantially the same terms as the lease then existing and as modified, and the trustee offered to make a new lease which should provide for a smaller net cash paym , but a larger percentage payment on gross sales.

[fol. 43] 8. One of the attorneys for The 415 Fifth Avenue Corporation told the attorney for the trustee within the next few days after January 28, 1944, that the character of the new management of the Childs Company, should there be a reorganization, was an important element to consider whether or not a lease might be accepted where a large part of the rental depended upon the earnings, and that that could not be known for some time, and that there was no hurry. Such statement by the attorney for The 415 Fifth Avenue Corporation to the attorney for the trustee was not known to this petitioner.

9. The petitioner did not authorize Birrell and Birrell or either one of them to act for him in this matter, nor did he represent or hold out to the trustee or to anyone representing the trustee that Birrell and Birrell or either one of them was authorized to act for him.

10. The petitioner did not authorize The 415 Fifth Avenue Corporation, H. Adams Ashforth, or Albert B. Ashforth, Incorporated to act for him in this matters nor did he hold out to the trustee or anyone in the trustee's behalf that any of those parties was so authorized.

11. On May 9, 1944, the attorney for the trustee sent a letter to the petitioner which is in evidence and marked Trustee's Exhibit D.

12. By this letter the attorney for the trustee meant by the expression that the trustee is desirous of assuming the lease of 1553 Broadway as modified that the trustee desired to make a new lease with the petitioner, which shall have substantially the same terms as Petitioner's Exhibit 1 in this case as modified by Petitioner's Exhibit 2.

[fol. 44] 13. This letter was not answered by the petitioner until June 1, 1944, when he wrote Petitioner's Exhibit 4, addressed to the trustee in this reorganization proceeding.

14. On June 23, 1944, the petitioner sent Petitioner's Exhibit 3 by registered mail to the trustee, John F. X. Finn, and to the Childs Company, the debtor, and said exhibit was received by each of said parties on that date or the day following.

15. On July 6, 1944, the attorney for the trustee sent to the petitioner Exhibit 5.

CONCLUSIONS OF LAW

16. The term for years granted under Exhibit 1 came to an end and terminated on August 26, 1943.

17. The petitioner is entitled to the relief prayed for.

Respectfully submitted, R. P. Stephenson, Special Master.

Dated: New York, N. Y., August 7, 1944.

[fol. 45] [Same Title]

OPINION OF SPECIAL MASTER ON PETITION OF BURTON C. MEIGHAN, JR., SUBSTITUTED TRUSTEE UNDER THE LAST WILL AND TESTAMENT OF WILLIAM T. WOOD, DECEASED

Petition of Burton C. Meighan, Jr., Substituted Trustee under the Last Will and Testament of William T. Wood, Deceased, for an order adjudging that the term granted by a certain lease is terminated and to direct the trustee forthwith to surrender possession of the premises involved. The answer of the trustee denies certain allegations of the petition and contains an affirmative defense which at the trial was amended so that paragraph number 13 thereof should read as follows:

"13. By virtue of the above facts, the petitioner has waived the provision in said lease purporting to

terminate the same and is estopped from asserting that the lease is terminated."

Meighan & Necarsulmer, Esqs., Louis A. Marchisio, Esq., Of counsel. For the petitioner.

Lorenz, Finn & Lorenz, Esqs., Joseph Lorenz, Esq., Of counsel. For the trustee.

Marshall, Bratter & Seligson, Esqs., Harold P. Seligson, Esq., Of counsel. For Childs Debenture Holders Committee.

[fol. 46] Stephenson, Special Master:

I will deal briefly in this opinion with the contentions of the parties on the law applicable to the facts in this case. The trustee contends that a literal construction of paragraph 4 of the lease is harsh and was not what the parties intended. There is much in the trustee's contention. The words used mean what the parties intended them to mean, though such meaning is not literally correct. Paragraph 4 enumerates a number of events which shall end the term of the lease. In stating that the term shall come to an end if the rent shall remain unpaid for more than ten days after written notice, the parties intended to mean a failure to pay for such ten days or a reasonable time thereafter if accepted by the landlord: that is the substance of the meaning in the actual facts of business transactions. The provision that the term shall came to an end if the tenant shall fail to perform any of the covenants, provisions, conditions or agreements contained means that if he shall substantially fail to an extent which might be injurious to the landlord. The provision that if a petition in bankruptcy shall be filed by the tenant or if the tenant shall be adjudged a bankrupt or insolvent by any court, means exactly what it says: for such events are, in and of themselves, of substantial importance to the landlord and to the tenant. The filing of a petition in bankruptcy by the tenant is an event which substantially affects not only temporarily, but for some time the ability of the tenant to meet its obligations under the lease. Adjudging a tenant a bankrupt likewise is a substantial and important matter. The adjudgment by a court that the bankrupt is insolvent (unable to pay its debts as they mature) is a substantial and

important matter to the landlord: for it substantially and materially affects the ability of the tenant to pay and to continue to pay during the balance of the term the rent [fol. 47] that may be due. The trustee contends that the word "insolvent" following the word "bankrupt" means insolvent in the bankruptcy sense. If this were an entirely new question, I would say there is much force in the trustee's argument, but that question has been decided by higher courts in cases that are substantially not any different from this one and I am bound to follow such decisions. The court held in re *Schulte Retail Stores Corporation*, 22 F. (Supp.) 612 that the word "insolvent" in a lease made in 1920 meant insolvent, not as defined in the Bankruptcy Act, but an inability to meet obligations as they mature. A similar decision was made as to the meaning of "insolvent" in re *Willow Cafeterias*, 95 F. (2nd) 306 and in re *Walker*, 93 F. (2nd), 281.

On August 26, 1943 the debtor filed a petition praying for relief under Chapter X of the Bankruptcy Act, and in such petition stated that it is unable to pay its debts as they mature. The Judge entered an order approving said petition. This is an adjudication that the debtor is unable to pay its debts as they mature. The Judge can only enter such an order if "satisfied that it" (the petition) "complies with requirements of this chapter" (Section 141). One of the requirements of the Chapter is that the petition shall state either that the debtor is insolvent or unable to pay its debts as they mature (Section 130). Therefore, the entering of an order approving the petition is an adjudication by the court that the debtor is unable to pay its debts as they mature. I must find that the tenant has been adjudged insolvent by a Court, and that on August 26, 1943, the date of the entry of the order approving the petition, this term came to an end.

The Trustee has the right to assume executory contracts, and with the permission of the judge to reject them (Section 116(1)). If the trustee assumed such contract, he would be assuming a contract without a term. Of [fol. 48] course he could do so, but it is not very likely he would, because he would then have liabilities and no rights.

This petitioner knew that there were negotiations with the adjoining landlord, and waited to see what would happen. He did no negotiating with the trustee, nor did he

authorize anyone to negotiate with the trustee: however, he stood by ready to accept anything which he thought might be advantageous.

Even if he could waive the termination of the lease, he did not do so. Furthermore, I do not see how he could waive termination if the effect of such waiver was to create a new lease. The term being an at an end, he cannot create a term for a longer period than a year except in writing signed by the party to be charged, and there was no writing in this case by any party to be charged.

Now, was there an estoppel? It is possible to create an interest in real estate by an estoppel. I do not believe that anything short of actual fraud or the conveying of property which a person doesn't have and later acquiring it can create an estoppel. I think there is no evidence of either in this case.

Dated: New York, N. Y., August 7, 1944.

[fol. 49] In United States District Court

[Same Title]

Objections to Special Master's Report on Petition of Burton C. Meighan, Jr., Substituted Trustee under the Last Will and Testament of William T. Wood, Deceased, With Respect to the Premises 1553 Broadway, New York, N. Y.

John F. X. Finn, Trustee of the above named Debtor, objects to the report of Hon. Robert P. Stephenson, Special Master herein, dated August 7, 1944, in the following particulars:

1. The conclusion of law (No. 16) that "the term for years granted under Exhibit 1 came to an end and terminated on August 26, 1943," is contrary to the evidence and is erroneous as a mater of law.

2. The conclusion of law (No. 17) that "the petitioner is entitled to the relief prayed for" is contrary to the evidence, and is erroneous as a matter of law.

Dated, New York, N. Y., September 27, 1944.

Lorenz, Finn & Lorenz, Attorneys for Trustee-Objector, 165 Broadway, New York N. Y.

[fol. 50] IN UNITED STATES DISTRICT COURT

[Same Title]

NOTICE OF MOTION TO CONFIRM REPORT OF SPECIAL MASTER

SIRS:

Please take notice that Burton C. Meighan, Jr., as Substituted Trustee under the Last Will and Testament of William T. Wood, Deceased, the owner in fee and landlord of premises known as and by 1553 Broadway, New York City, and as such the petitioner herein, will move this Court on the 23rd day of August, 1944, at ten thirty o'clock in the forenoon, or as soon thereafter as counsel can be heard, at the United States Court House, Foley Square, Borough of Manhattan, City of New York, Room 506, for an order confirming the report of Robert P. Stephenson, Esq., Special Master, filed herein on the 7th day of August, 1944, and adopting the findings of fact and conclusions of law of the said Special Master as the findings of fact and conclusions of law of this Court, and for such other and further relief as to this Court may seem proper and just in the premises.

Dated: New York City, August 10, 1944.

Yours, etc. Meighan & Necarsulmer, Attorneys for Petitioner, By Burton C. Meighan, Jr., Member of said firm, Office and P. O. Address, No. 120 Broadway, Borough of Manhattan, City of New York.

[fol. 51] To Lorenz, Finn & Lorenz, Esqs., Attorneys for John F. X. Finn, Trustee of Childs Company, 165 Broadway, New York, N. Y. And all other Parties in Interest.

In United States District Court, Southern District of New York

[Same title]

In re: Lease on 1553 Broadway, New York City

Petition of Burton C. Meighan, Jr., Substituted Trustee under the Last Will and Testament of William T. Wood, Deceased.

Opinion

Edward A. Conger, U. S. D. J.:

The Petitioner herein Burton C. Meighan, Jr. as substituted Trustee under the Last Will and Testament of William T. Wood, Deceased (Landlord) has petitioned this Court for an order adjudging that the term granted by and under a certain lease has terminated.

Petitioner is the Landlord of certain premises known as No. 1553 Broadway, New York City. The Debtor Childs Company has been occupying and using said premises, in connection with another property at No. 1551 Broadway, as a restaurant.

[fol. 52] Debtor's occupancy was pursuant to a lease which expired by its terms on April 30, 1947, with an option to renew, under certain terms and conditions, for a further period of 21 years.

On or about August 26, 1943 the Childs Company filed its petition herein for reorganization under Chapter X of the Bankruptcy Act. On the same day this Court approved the petition and appointed John F. X. Finn, Trustee of the Debtor; thereupon the said Trustee took possession of said premises and has been in possession and control of said premises ever since, as such Trustee.

The original lease contained the following provisions:

"4. The Tenant covenants that * * * if a petition in bankruptcy shall be filed by the tenant or if the tenant shall be adjudged bankrupt or insolvent by any Court, or if a trustee in bankruptcy of the tenant shall be appointed in any suit or proceeding brought

by or against the tenant, then and in each and every case, the term hereby granted shall immediately cease, determine and come to an end, and the landlord may recover and resume possession of the demised premises by any legal means."

"Recovery of Possession in Default

"13. * * * if a petition in bankruptcy shall be filed by the tenant or if the tenant shall be adjudged insolvent by any Court or if a Trustee in Bankruptcy of the tenant shall be appointed in any suit or proceeding by or against the tenant * * * the landlord may recover and assume possession of the demised premises by force or otherwise without being liable to prosecution therefor."

Petitioner, contending that the filing and approval of the Petition for reorganization is within the prohibition [fol. 53] of the above clauses and constituted a breach of the terms of the lease, asks that it be decreed that the lease has terminated and that Debtor and the Trustee be ordered to surrender the premises to Petitioner. The petition duly came before me. The Trustee denied certain material allegations of the petition and set up an affirmative defense of waiver of the right to cancel the lease on Petitioner's part.

I referred the whole matter to Robert P. Stephenson, as Special Master to hear and report. The Special Master heard the evidence on the issues presented and has handed down his Findings of Fact and Conclusions of Law, together with an opinion.

The Special Master has found against the debtor and in favor of Petitioner.

Petitioner has now moved to confirm the Report of the Special Master. The Trustee objects to the confirmation of the report and its adoption by this Court.

The Trustee's sole contention is that the filing of the Petition in Chapter X and its approval was not a violation of the terms of the lease.

The issue presented is a pure legal question. I realize that forfeitures are not favored by the Courts, but I have come to the conclusion that legally Petitioner is correct in his contention.

I agree in the main with the opinion of the Special Master.

The Trustee insists that the word "insolvent" as used in Paragraph 4 of the lease means insolvent in the Bankruptcy sense. *The sentence to* be construed reads: "or if the tenant *shall be adjudged bankrupt or insolvent by any court.*" The Trustee urges that the position of the words "bankrupt or insolvent" indicates that the draftsman of the instrument intended the two words to be synonymous. He urges that the word "insolvent" in Paragraph 4 follows language which concerns itself solely with bank-[fol. 54] ruptcy and that the phrase following concerns itself solely with bankruptcy. The Trustee contends that the construction rule of "ejusdem generis" applies. At first blush it would appear as though there might be some merit in the Trustee's argument.

I think however, his argument is too finely spun. When the Petition was approved it was adjudicated as to the debtor that "it was unable to pay its debts as they mature." It has been held that the word "insolvent" in a lease in a similar clause, as found here, means an inability to meet obligations as they mature.

Schulte Retail Stores Corporation, 22 Fed. Supp. 612 Affirmed;
In re Walker, et al., 98 Fed. (2) 281;
In re Wil-Low Cafeterias, Inc., 95 Fed. (2) 306.

In *In re Walker, supra*, we find the following pertinent language on page 283:

> "The insolvency mentioned in the lease cannot have been other than a failure to meet the lessee's obligations as they matured; that is the insolvency which throws the lessor's relations into confusion, delays payment of the rent, impounds his property for an indefinite time and in general makes it important for him to be free to reenter."

It should be noted that the lease was a New York contract. This is important in determining what the intention of the parties was. Certainly the words "*insolvent in any court*" indicate that the parties must have had in mind insolvency as defined by the laws of the State of New York (an inability to meet obligations as they mature) and not

insolvency in bankruptcy. Certainly the words "in any court" would seem to indicate that in the minds of the parties there was an intention to include within the bounds [fol. 55] of the clause of the lease a financial condition not measured by the rule of Federal Bankruptcy as exercised in the Federal Courts.

I agree with Judge Knox (Schulte Retail Stores Corporation, supra). "Hence, 'insolvent' must be taken to apply to situations not precisely within the purview of a bankruptcy proceeding * * * and inability to meet obligations as they matured was just such a situation."

The Report of the Special Master is confirmed and his Findings of Fact and Conclusions of Law adopted, as the Findings of Fact and Conclusions of Law of this Court.

The relief asked for in the petition herein is granted.

Settle order on five days' notice.

Edward A. Conger, United States District Judge.

Dated September 18, 1944.

[fol. 56] In United States District Court, Southern District of New York

[Same Title]

Order Confirming Report of Special Master In re Premises 1553 Broadway, New York, N. Y.

The petition of Burton C. Meighan, Jr., as substituted trustee under the last will and testament of William T. Wood, deceased, verified June 27, 1944, praying for an order adjudging that the term granted to Childs Company, the Debtor herein, by an indenture of lease dated July 31, 1922, as modified in certain respects by an agreement dated March 23, 1942, has terminated and come to an end and authorizing and directing the said debtor and John F. X. Finn, trustee of said debtor, to forthwith surrender possession of premises known as and by 1553 Broadway, New York City, to said petitioner, having duly and regularly come on to be heard on July 25, 1944, and due notice of said application having been given as prescribed by this Court by its order to show cause dated July 6, 1944, and the issues of fact raised by said petition and the an-

swering affidavit of Joseph Lorenz, sworn to July 24, 1944, and the affidavit of John F. X. Finn, trustee of the said debtor, sworn to July 24, 1944, and the affidavit of Kenneth LaBarre, sworn to July 24, 1944, having been referred to the Honorable Robert P. Stephenson, as Special Master, to hear the proofs and arguments of the parties and to report his findings of fact and conclusions of law thereon to this Court with all convenient speed pursuant to an order of this Court dated July 26, 1944, and the report of the said Special Master having been duly filed herein on August 7, 1944, and the petitioner herein having duly moved this Court for an order confirming the said report of Honor-
[fol. 57] able Robert P. Stephenson, Special Master, and adopting the findings of fact and conclusions of law of the Special Master as the findings of fact and conclusions of law of this Court, and after hearing Meighan & Necarsulmer, Esqs., attorneys for Burton C. Meighan, Jr., as Substituted Trustee as aforesaid, in support of the aforesaid application and Lorenz, Finn & Lorenz, attorneys for the Trustee of the debtor herein, and Marshall, Bratter & Seligson, attorneys for Protective Committee, etc., in opposition thereto, and due deliberation having been had thereon, and the opinion of this Court having been filed herein;

Now, upon the petition of Burton C. Meighan, Jr., as Substituted Trustee as aforesaid, the answer of John F. X. Finn, as Trustee of Childs Company, debtor, verified July 28, 1944, the report and opinion of Honorable Robert P. Stephenson, as Special Master, and the testimony taken upon the hearings before said special master, the exhibits and all other papers filed and proceedings had in connection with the said petition and hearing, it is

Ordered that the said report of Honorable Robert P. Stephenson, as Special Master, be and the same hereby is confirmed in all respects and the findings of fact and conclusions of law contained therein are hereby adopted as the findings of fact and conclusions of law of this Court, and it is further

Ordered, that the term for years granted Childs Company by a certain indenture of lease dated July 31, 1922, and as modified in certain respects by an agreement dated March 23, 1942, covering the premises known as and by 1553 Broadway, Borough of Manhattan, New York City, came to an end and terminated on August 26, 1943, and that

[fol. 58] the Childs Company, the debtor herein, and John F. X. Finn, trustee of the said debtor, be and they hereby are authorized and directed to surrender possession of said premises within thirty (30) days from September 27, 1944 to Burton C. Meighan, Jr., as Substituted Trustee under the Last Will and Testament of William T. Wood, deceased, and to remove from the said premises all property of the said debtor and the debtor's trustee, except fixtures and other articles of personal property attached to the building on the premises constituting a part of the realty or becoming the property of the petitioner under and pursuant to the terms of the aforesaid indenture of lease.

Dated, September 27th, 1944.

Edward A. Conger, U. S. D. J.

(Filed in the office of the Clerk on October 2, 1944.)

[fol. 59] In United States District Court

[Title omitted]

Notice of Appeal in re Premises 1553 Broadway, New York, N. Y.

Sirs:

Notice is hereby given, that John F. X. Finn, as Trustee of Childs Company, the above named Debtor, hereby appeals to the Circuit Court of Appeals for the Second Circuit from the Order of the United States District Court for the Southern District of New York, granting the petition of Burton C. Meighan, Jr., as Substituted Trustee under the Last Will and Testament of William T. Wood, Deceased, verified June 27, 1944, and directing that the Childs Company, Debtor herein, and John F. X. Finn, as Trustee of said Debtor, surrender possession of the premises known as 1553 Broadway, New York, N. Y., to the aforesaid Burton C. Meighan, Jr., as said Substituted Trustee, which Order was entered in this proceeding on October 2nd, 1944.

Dated, October 3rd, 1944.

Lorenz, Finn & Lorenz, By Joseph Lorenz, Attorneys for Appellant, John F. X. Finn, as Trustee of Childs Company, 165 Broadway, New York, N. Y.

[fol. 60] To Meighan & Necarsulmer, Esqs., Attorneys for Appellee, Burton C. Meighan, Jr., as Substituted Trustee under the Last Will and Testament of William T. Wood, Deceased, 120 Broadway, New York, N. Y.

Birrell & Birrell, Esqs., Attorneys for The 415 Fifth Avenue Company, Inc., 545 Fifth Avenue, New York, N. Y.

And all other Parties in Interest.

[fol. 61] In United States District Court

[Same Title]

Stipulation as to Record

It is Hereby Stipulated and Agreed that the foregoing is a true copy of the transcript of the record of the said District Court for the Southern District of New York, in the above entitled matter as agreed upon by the parties.

Dated, New York, N. Y., November 29, 1944.

Meighan & Necarsulmer, Attorneys for Burton C. Meighan, Jr., as Substituted Trustee under the Last Will and Testament of William T. Wood, Deceased, Appellee; Lorenz, Finn & Lorenz, Attorneys for John F. X. Finn, as Trustee of Childs Company, Appellant.

[fol. 62] Clerk's Certificate to foregoing transcript omitted in printing.

[fol. 63] UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT, OCTOBER TERM, 1944

No. 206

(Argued December 7, 1944. Decided December 28, 1944).

BURTON C. MEIGHAN, JR., as Substituted Trustee under the Last Will and Testament of William T. Wood, Deceased, Petitioner-Appellee,

against

JOHN F. X. FINN, as Trustee of Childs Company, Respondent-Appellant

Before Swan, Augustus N. Hand and Chase, Circuit Judges

Appeal from the District Court of the United States for the Southern District of New York

Proceedings for reorganization of Childs Company under Chapter X of the Bankruptcy Act. From an order therein adjudging that a lease held by the debtor came to an end on August 26, 1943, and directing that the debtor's trustee surrender possession to the lessor, said trustee has appealed. Affirmed.

[fol. 64] Lorenz, Finn & Lorenz, attorneys for appellant; Joseph Lorenz, of counsel.

Meighan & Necarsulmer, attorneys for appellee; Burton C. Meighan, Jr., and Louis A. Marchisio, of counsel.

SWAN, Circuit Judge:

This appeal involves a lease on 1553 Broadway in which the debtor conducts a restaurant in connection with the adjacent premises involved in the companion appeal decided herewith under the title of The 415 Fifth Avenue Company, Inc. v. Finn. The lease now under consideration was made in 1922 for a term of years expiring April 30, 1947. It contains provisions by virtue of which the lessor contends that the term came to an end on August 26, 1943. On that date the lessee filed its petition for reorganization and in such petition stated that it is unable to pay its debts as they mature. On the same date the court approved the petition and appointed the appellee as the debtor's trustee. On June

23, 1944 the lessor gave written notice to the debtor's trustee that the lease "has ceased, determined and come to an end by virtue of the bankruptcy proceedings now pending * * * relating to the said Childs Company." This was followed by the lessor's petition upon which the court adjudged that the lease did terminate on August 26, 1943. The provisions of the lease relevant to that decision read as follows:

"Conditional Limitation

4. The tenant covenants that if the rent reserved by this lease or any part thereof shall remain unpaid for more than ten days after written notice that it has become due or if the tenant shall fail to perform any [fol. 65] of the covenants, conditions, provisions, and agreements herein contained, or, if a petition in bankruptcy shall be filed by the tenant or if the tenant shall be adjudged bankrupt or insolvent by any Court, or if a trustee in bankruptcy of the tenant shall be appointed in any suit or proceeding brought by or against the tenant, then and in each and every such case, the term hereby granted shall immediately cease, determine and come to an end, and the landlord may recover and resume possession of the demised premises by any legal means.

* * * * * * *

Recovery of Possession on Default

13. The tenant covenants that if the rent reserved by this lease, or any part thereof, shall remain unpaid for more than ten days after written notice that same has become due, or the tenant shall fail to perform any covenant, condition, provision or agreement herein contained or if a petition in bankruptcy shall be filed by the tenant or if the tenant shall be adjudged insolvent by any Court, or if a trustee in bankruptcy of the tenant shall be appointed in any suit or proceeding by or against the tenant, or if the tenant shall be dispossessed or if the demised premises shall become vacant or abandoned, the landlord may recover and resume possession of the demised premises by force or otherwise, without being liable to prosecution therefor. * * *"

The sole issue presented by this appeal is whether the district court was correct in construing the clause "if the tenant shall be adjudged bankrupt or insolvent by any court" to apply to the order of the bankruptcy court approving the debtor's petition in reorganization and appointing a trustee. The appellant contends that "insolvent" as used in paragraph 4 of the lease refers to insolvency in the [fol. 66] bankruptcy sense, that is, to an excess of liabilities over assets rather than an inability to meet obligations as they mature. But such a construction would deprive the words "or insolvent by any court" of all utility; they would add nothing to the preceding words "adjudged bankrupt." Moreover in paragraph 13 the phrase "or if the tenant shall be adjudged insolvent by any court" is treated as a condition distinct and different from the filing by the tenant of a petition in bankruptcy, or from the appointment of a trustee in bankruptcy in any suit or proceeding by or against the tenant. In construing a contract the court should adopt a construction, if reasonable, which gives meaning to every word the parties use. Since the time-honored meaning of insolvency, in the absence of a statute specifying another meaning, is inability to meet obligations as they mature in ordinary course of business, it is entirely reasonable to suppose that the parties used "insolvent" in that sense rather than in the limited sense already covered by "adjudged bankrupt." *In re Wil-low Cafeterias, Inc.*, 22 F. Supp. 617, 619, Rev'd on another ground, 95 F. 2d 306 (C. C. A. 2), cert. den. 304 U. S. 567; *In re Schulte Retail Stores Corp.*, 22 F. Supp. 612 aff'd, *In re Walker*, 93 F. 2d 281 (C. C. A. 2); *Model Dairy Co., Inc.* v. *Foltis-Fischer, Inc.*, 67 F. 2d 704 (C. C. A. 2). It is true, as appellant urges, that in these cases the forfeiture clauses were more detailed than is the clause now under consideration; and it is likewise true, as was said in the *Model Dairy* opinion, *supra*, that such clauses are not viewed with "a friendly eye." But we do not think the rule of strict construction would justify reading all meaning out of the words which follow, "adjudged bankrupt," in paragraph 4 of the lease. "* * * We must give effect to the fair meaning of the language used." *Model Dairy* case, *supra*, at page 706. The order is affirmed.

[fol. 67] UNITED STATES CIRCUIT COURT OF APPEALS, SECOND CIRCUIT

At a Stated Term of the United States Circuit Court of Appeals, in and for the Second Circuit, held at the United States Courthouse in the City of New York, on the 18th day of January one thousand nine hundred and forty-five.

Present: Hon. Thomas W. Swan, Hon. Augustus N. Hand, Hon. Harrie B. Chase, Circuit Judges.

In the Matter of

CHILDS COMPANY, Debtor, BURTON C. MEIGHAN, JR., etc., Appellee,

JOHN F. X. FINN, as Trustee, etc., Appellant

Appeal from the District Court of the United States for the Southern District of New York

This cause came on to be heard on the transcript of record from the District Court of the United States for the Southern District of New York, and was argued by counsel.

On Consideration Whereof, it is now hereby ordered, adjudged, and decreed that the order of said District Court be and it hereby is affirmed with costs.

It is further ordered that a Mandate issue to the said District Court in accordance with this decree.

Alexander M. Bell, Clerk.

[fols. 68-69] [Endorsed:] United States Circuit Court of Appeals, Second Circuit. In re Childs Company, Debtor, Burton C. Meighan, Jr., etc., Appellee, John F. X. Finn, as Trustee, etc., Appellant. Order for Mandate. United States Circuit Court of Appeals, Second Circuit. Filed Jan. 18, 1945. Alexander M. Bell, Clerk.

[fol. 70] SUPREME COURT OF THE UNITED STATES

ORDER ALLOWING CERTIORARI—Filed March 5, 1945

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Second Circuit is granted, and the case is transferred to the summary docket. Counsel are requested to discuss in their briefs and upon oral argument the question whether the construction of the contract is governed by federal or state law.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

Endorsed on Cover: Enter Joseph Lorenz, File No. 49,406. U. S. Circuit Court of Appeals, Second Circuit. Term No. 953. John F. X. Finn, as Trustee of Childs Company, Petitioner, vs. Burton C. Meighan, Jr., as Substituted Trustee under the last will and testament of William T. Wood, Deceased. Petition for a writ of certiorari and exhibit thereto. Filed February 17, 1945. Term No. 953 O. T. 1944.

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CLERK

IN THE

Supreme Court of the United States

October Term, 1944 — No. 953

IN THE MATTER

OF

CHILDS COMPANY, DEBTOR

In Proceedings for Reorganization under Chapter X of the Bankruptcy Act — No. 82,868

JOHN F. X. FINN, as Trustee of CHILDS COMPANY
Petitioner

against

BURTON C. MEIGHAN, Jr., as Substituted Trustee under the Last Will and Testament of William T. Wood, Deceased
Respondent

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT and BRIEF IN SUPPORT OF PETITION

LORENZ, FINN & LORENZ
Attorneys for Petitioner
165 Broadway
New York 6, New York

JOSEPH LORENZ
Of Counsel

307 BAR PRESS, INC., 47 WEST ST., NEW YORK. BO. 9—0157 - 8

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IN THE

Supreme Court of the United States

October Term, 1944 — No.

In the Matter

of

CHILDS COMPANY, DEBTOR.

In Proceedings for Reorganization under Chapter X of the Bankruptcy Act — No. 82,868

JOHN F. X. FINN, as Trustee of CHILDS COMPANY,
Petitioner,

against

BURTON C. MEIGHAN, JR., as Substituted Trustee under the Last Will and Testament of William T. Wood, Deceased,
Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

Your petitioner, John F. X. Finn, as Trustee of Childs Company, respectfully prays for a writ of certiorari to the Circuit Court of Appeals for the Second Circuit to review a decree of that Court entered in the above entitled proceeding on January 18, 1945, affirming an Order of the United States District Court, dated September 27, 1944, which granted a petition of the respondent and adjudged that all rights of petitioner and of Childs Company under

an indenture of lease dated July 31, 1922, as modified, covering premises at 1553 Broadway, New York City, had terminated and come to an end (R. 66).

Neither the opinion herein of the United States District Court for the Southern District of New York nor the opinion of the Circuit Court of Appeals for the Second Circuit has yet been reported.

I

Summary and Short Statement of the Matter Involved

Childs Company, the Debtor herein, is engaged in the business of operating a chain of restaurants. It has been a lessee of, and has operated a restaurant upon, the premises at 1553 Broadway, New York City, for more than 40 years. On July 31, 1922, the Debtor entered into a lease with a predecessor of the respondent landlord for a period of twenty-one years from May 1, 1926 to April 30, 1947 covering said premises (R. 7). (The lease was subsequently modified in respects not pertinent here.) The Debtor has a heavy investment in improvements and equipment in the leasehold (R. 22). Said lease contains the following provision (R. 7-8):

> "4. The tenant covenants that * * * if a petition in bankruptcy shall be filed by the tenant or if the tenant shall be adjudged bankrupt or insolvent by any Court, or if a trustee in bankruptcy of the tenant shall be appointed in any suit or proceeding brought by or against the tenant, then and in each and every such case, the term hereby granted shall immediately cease, determine and come to an end, and the landlord may recover and resume possession of the demised premises by any legal means."

On August 26, 1943, the Debtor filed a voluntary petition for its reorganization under Chapter X of the Bankruptcy Act, in the United States District Court for the

Southern District of New York, and on that day John F. X. Finn was appointed Trustee of the Debtor by order of said Court (R. 42). The petition for reorganization stated that the Debtor was unable to pay its debts as they matured (R. 42).

On May 9, 1944, the attorney for the Trustee of the Debtor wrote the landlord stating that the Trustee was desirous of assuming the lease at 1553 Broadway, New York, as modified (R. 40).

On June 23, 1944, the Trustee received a notice from the landlord stating that said lease "has ceased, determined and come to an end by virtue of the bankruptcy proceedings now pending in the United States District Court, Southern District of New York, relating to the Childs Company" (R. 35).

Immediately thereafter, by petition verified June 27, 1944, Burton C. Meighan, Jr., the respondent landlord, brought a petition in the United States District Court, for the Southern District of New York, for an order adjudging that the lease of the Debtor had terminated (R. 6-10). The ground upon which the landlord based his petition was the filing of the petition for reorganization, as above set forth, and the appointment by the Court of petitioner as Trustee of the Debtor, which the landlord claimed was in violation of the forfeiture provision of the lease.

The courts below have held that the filing of the petition for reorganization containing the allegation that the Debtor was unable to meet its debts as they matured, and the appointment of the Trustee of the Debtor, pursuant to said petition, constituted an adjudication that the Debtor was "insolvent", in violation of the above quoted forfeiture provision of the lease, and that the lease had therefore automatically terminated on the day of the Trustee's appointment. The correctness of this determination presents an issue of law which is the sole question in this case.

An order staying the mandate of the Circuit Court of Appeals, pending application for certiorari, was granted by Mr. Justice Jackson on February 9, 1945.

II

Reasons Relied Upon for the Granting of the Writ of Certiorari

1. The decision of the Circuit Court of Appeals for the Second Circuit in the instant case is in direct conflict with the decision of the Circuit Court of Appeals for the Sixth Circuit in *Simmons* v. *National Tool Co.*, 110 Fed. (2d) 850. This conflict between the Circuits involves an important principle affecting corporation reorganizations and should be determined by the Supreme Court.

2. The decision of the Circuit Court of Appeals for the Second Circuit in the present case would seriously impede the administration of corporate reorganizations under Chapter X of the Bankruptcy Act and thwart the purpose of the statute in many instances.

3. The decision by the Circuit Court of Appeals for the Second Circuit violates fundamental and general rules of construction with respect to forfeiture clauses in leases or other contracts, and has given the phrase in question in the lease an unjustifiable construction.

WHEREFORE your petitioner prays that a writ of certiorari be issued under the seal of this Court, directed to the United States Circuit Court of Appeals for the Second Circuit to the end that this cause may be reviewed and determined by this Court; that the decree of the Circuit Court of Appeals for the Second Circuit be reversed; and that petitioner be granted such other and further relief as may be just and proper.

Dated: New York, February 15, 1945.

JOSEPH LORENZ
Counsel for Petitioner

IN THE

Supreme Court of the United States

October Term, 1944 — No.

In the Matter

of

CHILDS COMPANY, DEBTOR.

In Proceedings for Reorganization under Chapter X of the Bankruptcy Act — No. 82,868

JOHN F. X. FINN, as Trustee of CHILDS COMPANY,
Petitioner,

against

BURTON C. MEIGHAN, JR., as Substituted Trustee under the Last Will and Testament of William T. Wood, Deceased,
Respondent.

BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI

I

The opinions below and the statement of the case are believed sufficiently set forth in the foregoing petition.

II. GROUNDS OF JURISDICTION

The jurisdiction of this Court is invoked under Section 240 of the Judicial Code, as amended by the Act of February 13, 1925 (28 U. S. C., Sec. 347) and Section 24 (c) of the Bankruptcy Act.

III. SPECIFICATION OF ERRORS

The Petitioner will urge that the Circuit Court of Appeals for the Second Circuit erred:

1. In holding that the filing by the Debtor of a voluntary petition for reorganization under Chapter X of the Bankruptcy Act in which it was alleged that the Debtor is unable to meet its debts as they matured and the entry of an order by the District Court approving the petition, constituted an adjudication that the Debtor was "insolvent" in violation of the forfeiture clause contained in the lease between the parties.

2. In holding that the term "insolvent" as contained in said lease was to be construed as meaning inability to pay debts as they mature, as distinct from insolvency in the bankruptcy sense.

3. In that the decision of the Circuit Court of Appeals violates fundamental and general rules of construction with respect to forfeiture clauses in leases or other contracts, and has given the phrase in question in the lease an unjustifiable construction.

4. In failing to reverse the order of the District Court decreeing that the lease between the parties was terminated and directing the petitioner and the Debtor to vacate the premises in question.

IV. SUMMARY OF ARGUMENT

The points of argument will follow the reasons relied upon for the Writ of Certiorari, and will be discussed in the order stated in the petition.

V. ARGUMENT

POINT I

The decision of the Circuit Court of Appeals for the Second Circuit in the instant case is in direct conflict with the decision of the Circuit Court of Appeals for the Sixth Circuit in *Simmons* v. *National Tool Co.*, 110 Fed. (2d) 850. This conflict between the Circuits involves an important principle affecting corporate reorganizations and should be determined by the Supreme Court.

On August 26, 1943, the Debtor herein filed its petition in the District Court for the Southern District of New York for corporate reorganization, alleging therein that it was unable to meet its obligations as they matured (R. 42). This allegation was required in order to comply with Section 130 of Chapter X to the effect that:

> "Every petition shall state (1) that the corporation is insolvent *or* unable to meet its debts as they mature." (Italics ours.)

Upon the same day, the District Court entered an order approving the filing of the petition and appointed a trustee of the Debtor (R. 42). The District Court (R. 54) and the Circuit Court of Appeals have decided that the filing of the voluntary petition for reorganization with the allegation by the Debtor that it was unable to meet its debts

as they matured, and the approval of the petition by the District Court, as is required by Chapter X, constituted an adjudication of insolvency within the meaning of the forfeiture clause contained in the lease.

The Court of Appeals in its opinion stated the issue presented as follows (R. 65):

> "The sole issue presented by this appeal is whether the district court was correct in construing the clause 'if the tenant shall be adjudged bankrupt or insolvent by any court' to apply to the order of the bankruptcy court approving the debtor's petition in reorganization and appointing a trustee. The appellant contends that 'insolvent' as used in paragraph 4 of the lease refers to insolvency in the bankruptcy sense, that is, to an excess of liabilities over assets rather than an inability to meet obligations as they mature."

The Court further stated:

> "Since the time-honored meaning of insolvency, in the absence of a statute specifying another meaning, is inability to meet obligations as they mature in ordinary course of business, it is entirely reasonable to suppose that the parties used 'insolvent' in that sense rather than in the limited sense already covered by 'adjudged bankrupt'."

The decision of the Circuit Court of Appeals for the Second Circuit in the instant case is in direct conflict with the decision of the Circuit Court of Appeals for the Sixth Circuit in *Simmons v. National Tool Co.*, 110 Fed. (2d) 850. In that case the National Tool Co. had a license under a patent to use certain grinding machines. The license contained a provision that "in the event of the bankruptcy, *insolvency* or dissolution of the National Tool Co., no title to said machines shall be vested in any receiver or trustee * * *" (italics ours). The National Tool

Co. filed a petition for relief under Section 77B of the Bankruptcy Act in which it alleged that "the Debtor is unable to meet its debts as they mature * * *". The patentee contended that the filing and approval of the petition constituted an adjudication of insolvency of the National Tool Co. which operated as a cancellation or termination of the license. This is precisely the same claim which was made by the landlord in the instant case. The Circuit Court of Appeals for the Sixth Circuit flatly rejected this contention, stating, at page 850:

> "* * * it being the view of the court that the reorganization under Section 77B does not involve 'bankruptcy, insolvency or dissolution' in the sense those terms are used in the license agreement".

An examination of the record in the *Simmons* case discloses that the appellant in that case relied upon the cases in the Second Circuit of *In re Wil-Low Cafeterias Inc.*, 95 Fed. (2d) 306 and *In re Walker*, 93 Fed. (2d) 281, which are the primary cases relied upon by the Circuit Court of Appeals for the Second Circuit in the case at bar. The Sixth Circuit obviously rejected the authority of said cases.

POINT II

The decision of the Circuit Court of Appeals for the Second Circuit in the present case would seriously impede the administration of corporate reorganizations under Chapter X of the Bankruptcy Act and thwart the purpose of the statute in many instances.

Chapter X of the Bankruptcy Act, commonly known as the Chandler Act, was enacted by Congress to provide a more satisfactory method for the reorganization of corporations which found themselves in temporary financial straits. Its purpose was to permit the business of such

corporations to be continued and their assets preserved for creditors and stockholders, rather than have them partially or wholly destroyed by proceedings in bankruptcy or equity receiverships. In innumerable instances, corporate contracts, including leases, constitute assets which, in many cases, are vital to the continuance of the business. Many such corporate contracts contain clauses of the type involved herein. If the decision of the Circuit Court of Appeals for the Second Circuit should in such situations be followed, the very filing and approval of the petition for reorganization would immediately operate to cancel such executory contracts and thus defeat in large part the very purpose of the reorganization proceedings, inasmuch as every voluntary petition for corporate reorganization must allege under Section 130 of the Act that the corporation is "insolvent *or that it is unable to meet its debts as they mature.*" The question presented is novel and has never been passed upon by this Court either with respect to Section 77B or its successor, Chapter X of the Bankruptcy Act. It involves a question of paramount importance in the administration of corporate reorganizations.

POINT III

The decision by the Circuit Court of Appeals for the Second Circuit violates fundamental and general rules of construction with respect to forfeiture clauses in leases or other contracts, and has given the phrase in question an unjustifiable construction.

It is axiomatic that courts of equity abhor a forfeiture, and that in the construction of forfeiture clauses, they have uniformly resolved any doubt against a forfeiture. This attitude is illustrated by the decision of this Court in *Gazlay* v. *Williams, Trustee, etc.*, 210 U. S. 41. In that case the question was whether the bankruptcy of a

tenant terminated a lease providing for its forfeiture "if said lessee shall assign this lease or underlet said premises, or any part thereof, or if said lessee's interest therein shall be sold under execution or other legal process, without the written consent of said lessors." The Supreme Court obviously applied the rule of strict construction, holding that the bankruptcy of the holder of the lease did not terminate it, notwithstanding that bankruptcy works an assignment by operation of law.

The same principle of strict construction has been applied by the Court of Appeals of the State of New York in *Francis* v. *Ferguson*, 246 N. Y. 516. There the Court stated in part:

> "An ordinary covenant against assignment does not bind the executors of the tenant, and is not broken by a transfer of the leased premises by operation of law, Squire *v.* Learned, 196 Mass. 134; 81 N. E. 880; 11 L. R. A. (N. S.) 634, 124 Am. St. Rep. 525, 12 Ann. Cas. 977; Gazlay *v.* Williams, 210 U. S. 41, 28 S. Ct. 687, 52 L. Ed. 950. The covenant may, however, be so drawn as expressly to prohibit such a transfer. To accomplish such a prohibition in case of a devolution to executors, *its language must be 'very special'*. Seers *v.* Hind, 1 Ves. Jr. 294. *Such covenants are construed 'with the utmost jealousy'*. Higgs *v.* Pursell, 66 N. Y. 193, 201." (Italics ours.)

Professor Williston states the rule simply:

> "Therefore construction of a contract which would lead to a forfeiture cannot be favored." (3 Williston on Contracts (1936) Sec. 620, p. 1787.)

Federal courts sitting in bankruptcy are vested with all the powers of courts of equity, and, as this Court has had occasion to state recently, will use such powers to effectuate an equitable result. Thus, in *Pepper* v. *Lytton*, 308 U. S. 295, this Court stated, at pages 304-305:

> "The bankruptcy courts have exercised these equitable powers in passing on a wide range of problems arising out of the administration of bankrupt estates. They have been invoked to the end that fraud will not prevail, that substance will not give way to form, that technical considerations will not prevent substantial justice from being done."

Bearing in mind the acknowledged principle that forfeiture clauses must be strictly construed, it would seem that the decision below in the instant case is unjustifiable.

In the first place, it is clear that under Chapter X itself, inability of a debtor to meet obligations as they mature does not constitute "insolvency". Chapter X, as we have seen, provides that a petition for reorganization shall state that "the debtor is insolvent *or* unable to meet its debts as they mature". Clearly the words "unable to meet its debts as they mature", mean something other than insolvent. Insolvency, moreover, is specifically defined in section 1, subdivision 19 of the Bankruptcy Act, as follows:

> "Whenever the aggregate of his property * * * shall not at a fair valuation be sufficient in amount to pay his debts:".

Obviously, therefore, from the point of view of Chapter X itself, the granting of the petition for reorganization on the ground that the Debtor was unable to meet its debts as they mature, did not constitute an adjudication that "the Debtor was insolvent."

The petitioner recognizes, of course, that the lease was entered into long before Chapter X was enacted. The same definition of insolvency, however,—namely, an excess of liabilities over assets, has been in the Bankruptcy Act since its inception.

We submit, moreover, that the parties intended to use the term "insolvent" as contained in the forfeiture clause in the lease in the bankruptcy sense. For convenience, said clause is repeated here (R. pp. 7-8):

> "4. * * * if a petition in bankruptcy shall be filed by the tenant or if the tenant shall be adjudged bankrupt or *insolvent* by any Court, or if a trustee in bankruptcy of the tenant shall be appointed in any suit or proceeding by or against the tenant, then and in each and every such case, the term hereby granted shall immediately cease, determine and come to an end, * * *." (Italics ours.)

It is submitted that the above clause was intended to cover all types of *bankruptcy* situations and that by the application of the rule of "ejusdem generis" which is palpably called for in the present situation, "insolvent" must be construed in the bankruptcy sense. The court below itself recognized the applicability of the rule that clauses providing for forfeitures must be strictly construed, but was of the opinion that its decision was necessitated in order to give "meaning to every word the parties use," that, therefore, a separate significance had to be given to the word "insolvent". The Court stated in this connection that "such a construction would deprive the words 'or insolvent by any court' of all utility; they would add nothing to the preceding word 'adjudged bankrupt' ". This contention, it would seem, contains a double fallacy. In the first place, by the rule of *ejusdem generis*, it has been frequently held that a number of words may be used to convey a similar meaning. Parties frequently use several words to convey the same idea. Indeed, in the very clause in question as above quoted, the parties stated that upon the happening of any of the grounds of forfeiture, "the term hereby granted shall immediately *cease, determine*, and *come to an end*." Can it be seriously urged that

separate meanings are to be attached to the respective words "cease", "determine" and "come to an end"? In the second place, there is in fact an obvious purpose in the use of the words "or insolvent", in addition to the word "bankrupt". The Federal courts have exclusive jurisdiction over bankruptcies in the administration of the National Bankruptcy Act. On the other hand, if, as has several times occurred in our history, no National Bankruptcy Act is in existence, then the respective State laws covering insolvencies are applicable. The State of New York has such an Insolvency Law. It is contained in sections 50 to 88, inclusive, of the New York Debtor and Creditor Law. This law has not been repealed by the enactment of the National Bankruptcy Act; it is merely suspended in operation. The undoubted purpose of the language in question was to provide that an adjudication of *insolvency* under the State Insolvency Law should constitute a forfeiture if there were no National Bankruptcy Act. Debtors under the National Bankruptcy Act are adjudicated *"bankrupt"*; under the State Insolvency Law, they are adjudicated *"insolvent"*. The State Insolvency Law does not use the word "bankrupt". It would seem clear, therefore, that the purpose of the additional phrase was to cover the contingency of proceedings under the New York Insolvency Law.

It is of fundamental importance, however, to note that the definition of insolvency under the New York Insolvency Law is *not* inability to meet obligations as they mature, but an *insufficiency of assets to meet debts*. Thus section 52 of the Debtor and Creditor Law, defining what a petition for an adjudication of insolvency must contain, states:

> "Sec. 52. *Contents of petition.*—The petition must be in writing; it must be signed by the *insolvent*, * * *; it must set forth, in substance, that *he is unable to pay all his debts in full*; * * * (italics ours).

We urge, therefore, that there was indeed a reason for the insertion of the words "or insolvent" after the words "adjudged bankrupt". That reason was to cover the contingency of an adjudication of insolvency under the State Insolvency Law in the absence of a Federal Bankruptcy Statute, but that the word "insolvent" as used in that State Statute *has precisely the same meaning as it has under the National Bankruptcy Act, namely, an insufficiency of assets to cover liabilities.*

In fact, wholly apart from the definition of insolvency in the sense of more liabilities than assets as used in the New York Insolvency Law, "insolvency" has been defined in the same way in New York in many other instances, both under the Common Law and by statute. Thus in *Kane* v. *Larkin*, 131 N. Y. 300, 307, 308, the Court of Appeals of New York as early as 1892, before the lease in question was made, stated (p. 307) in a case involving a fraudulent conveyance, that:

> "If the grantor remains insolvent after the conveyance and *has sufficient property left to satisfy all his debts*, then the conveyance, whatever his intention cannot be a fraud upon his existing creditors." (Italics ours.)

And again:

> "But the person assailing the deed assumes the burden of showing that it was executed in bad faith and that it left the grantor insolvent and *without ample property to pay his existing debts and liabilities* and so it has been repeatedly held." (Italics ours.)

Similar definitions of insolvency are contained in Section 101 of the Debtor and Creditor Law of the State of New York and in Section 955 of the Penal Law.

It would seem, therefore, that there is no basis for concluding that the parties had any definition of insolvency in mind other than insolvency in the sense of greater liabilities than assets. *To say the very least, there is an ambiguity.* That being the case, since a forfeiture is involved, the ambiguity should be resolved in favor of the tenant.

CONCLUSION

It is respectfully submitted that the petition for certiorari should be granted.

Dated: February 15, 1945.

JOSEPH LORENZ
Counsel for the Petitioner

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IN THE

Supreme Court of the United States

October Term, 1944 — No. 953

JOHN F. X. FINN, as Trustee of CHILDS COMPANY
Petitioner

against

BURTON C. MEIGHAN, Jr., as Substituted Trustee under the Last Will and Testament of William T. Wood, Deceased
Respondent

PETITIONER'S BRIEF

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

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3 Williston on Contracts (1936), Section 620, p. 1787	16
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IN THE

Supreme Court of the United States

October Term, 1944 — No. 953

JOHN F. X. FINN, as Trustee of Childs Company,
Petitioner,

against

BURTON C. MEIGHAN, JR., as Substituted Trustee under the Last Will and Testament of WILLIAM T. WOOD, Deceased.

BRIEF ON BEHALF OF PETITIONER

I. OPINIONS BELOW

The opinion below of the Circuit Court of Appeals for the Second Circuit (R. 43-45) is officially reported in 146 Fed. 2d, 594. The opinion rendered by the District Court for the Southern District of New York (R. 36-39) has not been officially reported.

II. JURISDICTION

The jurisdiction of this Court is invoked pursuant to Section 240 of the Judicial Code, as amended by the Act of February 13, 1925 (28 U. S. C., Section 347) and Section 24(c) of the Bankruptcy Act.

III. STATEMENT OF CASE

Childs Company, the Debtor herein, is engaged in the business of operating a chain of restaurants. It has been a lessee of, and has operated a restaurant upon, the premises at 1553 Broadway, New York City, for more than 40 years. On July 31, 1922, the Debtor entered into a lease with a predecessor of the respondent landlord for a period of twenty-one years from May 1, 1926 to April 30, 1947 covering said premises (R. 5). (The lease was subsequently modified in respects not pertinent here.) The Debtor has a heavy investment in improvements and equipment in the leasehold (R. 17). Said lease contains the following provision (R. 5):

> "4. The tenant covenants that * * * if a petition in bankruptcy shall be filed by the tenant or if the tenant shall be adjudged bankrupt or insolvent by any Court, or if a trustee in bankruptcy of the tenant shall be appointed in any suit or proceeding brought by or against the tenant, then and in each and every such case, the term hereby granted shall immediately cease, determine and come to an end, and the landlord may recover and resume possession of the demised premises by any legal means."

On August 26, 1943, the Debtor filed a voluntary petition for its reorganization under Chapter X of the Bankruptcy Act, in the United States District Court for the Southern District of New York, and on that day the Judge entered an order approving the petition, and appointed John F. X. Finn trustee of the Debtor (R. 29). The petition for reorganization stated that the Debtor was unable to pay its debts as they matured (R. 29).

On May 9, 1944, the attorney for the Trustee of the Debtor wrote the landlord stating that the Trustee was desirous of assuming the lease at 1553 Broadway, New York, as modified (R. 28).

On June 23, 1944, almost ten months after the Trustee's appointment, the Trustee received a notice from the landlord stating that the lease "has ceased, determined and come to an end by virtue of the bankruptcy proceedings now pending in the United States District Court, Southern District of New York, relating to the Childs Company" (R. 25).

Immediately thereafter, by petition verified June 27, 1944, Burton C. Meighan, Jr., the respondent landlord, brought a petition in the United States District Court for the Southern District of New York, for an order adjudging that the lease of the Debtor had terminated (R. 4-7). The ground upon which the landlord based his petition was the filing of the petition for reorganization, as above set forth, and the appointment by the Court of petitioner as Trustee of the Debtor, which the landlord claimed was in violation of the forfeiture provision of the lease.

The courts below have held that the filing of the petition for reorganization containing the allegation that the Debtor was unable to meet its debts as they matured, and the appointment of the Trustee of the Debtor, pursuant to said petition, constituted an adjudication that the Debtor was "insolvent", in violation of the above quoted forfeiture provision of the lease, and that the lease had therefore automatically terminated on the day of the Trustee's appointment. The correctness of this determination presents an issue of law which is the sole question in this case.

The Trustee's petition for certiorari was granted by this Court, and the order thereon was filed on March 5, 1945 (R. 47). The order stated that "Counsel are requested to discuss in their briefs and upon oral argument the question whether the construction of the contract is governed by federal or state law" (R. 47).

IV. SPECIFICATION OF ERRORS

The Petitioner urges that the Circuit Court of Appeals for the Second Circuit erred:

1. In holding that the filing by the Debtor of a voluntary petition for reorganization under Chapter X of the Bankruptcy Act in which it was alleged that the Debtor is unable to meet its debts as they matured and the entry of an order by the District Court approving the petition, constituted an adjudication that the Debtor was "insolvent" in violation of the forfeiture clause contained in the lease between the parties.

2. In holding that the term "insolvent" as contained in said lease was to be construed as meaning inability to pay debts as they mature, as distinct from insolvency in the bankruptcy sense.

3. In that the decision of the Circuit Court of Appeals violates fundamental and general rules of construction with respect to forfeiture clauses in leases or other contracts, and has given the phrase in question in the lease an unjustifiable construction.

4. In failing to reverse the order of the District Court decreeing that the lease between the parties was terminated and directing the petitioner and the Debtor to vacate the premises in question.

V. SUMMARY OF ARGUMENT

The construction and effect of the clause in the lease, providing that the lease is automatically forfeited if the tenant is "adjudged * * * insolvent", directly involves the policy, administration, and interpretation of the Chandler Act. The fundamental purpose of Chapter X of that Act would in many cases be thwarted if valuable, and often

vital, assets were lost by the very fact of the institution of reorganization proceedings designed to conserve the debtor's property. Accordingly, under the principles laid down in *Prudence Corp.* v. *Geist*, 316 U. S. 89, the Federal law governs the construction of the forfeiture clause.

A definite Federal policy, as typified by this Court's decision in *Gaslay* v. *Williams*, 210 U. S. 41, and by pertinent provisions in Section 70b of the Bankruptcy Act, decrees that a forfeiture clause in a lease, which would deprive a debtor's estate of valuable assets by the fact of the institution of bankruptcy or reorganization proceedings should be most strictly construed. Although explicit and unequivocal forfeiture clauses may be enforcible, yet the Federal policy is so strong against such forfeiture clauses that they will not be given effect unless the condition for forfeiture upon which the landlord relies is unmistakably set forth.

The case of *Simmons* v. *National Tool Co.*, 110 Fed. (2d) 850 (C. C. A. 6) is directly in point, and contra to the decision of the Court below.

The Circuit Court of Appeals in the present case rested its decision primarily upon the proposition that every word in a contract should be given a separate and distinct meaning; it concluded, therefore, that in the phrase "adjudged bankrupt or insolvent by any Court", "insolvent" meant inability to meet debts as they mature, because, it claimed, a different view would involve "reading all meaning out" of the word. This reasoning, petitioner contends, contains a double fallacy. The forfeiture clause must be construed as a whole, and so construed, it appears that the clause is concerned only with bankruptcy proceedings and that "insolvent" is used in the bankruptcy sense of liabilities exceeding assets. The clauses which both precede and follow the phrase in question, deal only with bankruptcy. The phrase itself "adjudged bankrupt or insolvent by any Court", following as it does, the clause relating to *voluntary* bankruptcy proceedings, should be reasonably con-

strued as referring to adjudications in *involuntary* proceedings. The evident preoccupation of the clause in its entirety with bankruptcy and the application of the rule of *"ejusdem generis"* lead to the conclusion that "adjudged bankrupt or insolvent" was merely an alternative or emphatic expression of the same idea; that bankruptcy proceedings only were contemplated by the clause; and that the word "insolvent" is used in the bankruptcy sense.

If, however, it should be deemed that the words "or insolvent" should be given a separate meaning or purpose, it by no means follows that the conclusion of the Circuit Court of Appeals that "insolvent" was used in the sense of inability to pay debts as they mature, is correct. The phrase "adjudged * * * insolvent by any Court" should in that event be reasonably construed to apply to an adjudication of insolvency under the insolvency law of New York, which is set forth in sections 50-88 inclusive of the Debtor and Creditor Law of that State. This law is merely suspended and not repealed by the enactment of the Federal Bankruptcy Act. The lease was for a long term; the landlord would naturally intend to receive the same protection if the tenant were "adjudged insolvent" under the cognate State insolvency law as he would receive if the tenant were "adjudged bankrupt" under the National Bankruptcy Act, if that were in existence. No proceedings have been had under the State insolvency law; no adjudication that the Debtor is "insolvent" has been made under that law; and, in fact, *that law defines insolvency in the same way as does the Federal Act, namely, more liabilities than assets.*

Finally, various other statutory provisions and decisions at common law in New York have defined "insolvency" in the bankruptcy sense; if that word be interpreted in the light thereof, petitioner's construction is fortified.

In any event, the least that can be said is that the phrase is ambiguous. That being so, in view not only of

the strong federal policy above referred to, but also of the universal policy of strict construction where forfeitures are involved, we submit that the conclusion is irresistible that the word "insolvent" must be construed in the bankruptcy sense.

VI. ARGUMENT

POINT I

The construction of the clause of the lease here involved is governed primarily by Federal law. Federal policy clearly requires a most strict construction of a forfeiture clause which would operate to deprive a debtor's estate of valuable property by the fact of the institution of reorganization proceedings.

The order of the Supreme Court granting certiorari stated that "Counsel are requested to discuss in their briefs and upon oral argument the question whether the construction of the contract is governed by federal or state law" (R. 47). It is petitioner's position that the Federal law is applicable; that the said law clearly requires the construction which we urge; but that even if the law of the State of New York be applied, that law likewise requires the adoption of petitioner's construction.

We recognize, of course, that a Court of Bankruptcy will normally apply the law of a state in the construction of contracts made and to be performed therein, and in the determination of property rights created by or dependent upon the law of that state. It has, however, definitely and repeatedly been decided by this Court that where the interpretation or administration of a federal statute is involved, the federal and not the local law applies. This is particularly true where the federal statute expresses a policy concerning the specific subject matter involved.

Prudence Realization Corporation v. Geist, 316 U. S. 89;

Wragg v. *Federal Land Bank of New Orleans*, 317 U. S. 325;
Sola Electric Co. v. *Jefferson Co.*, 317 U. S. 173.

In considering the problem, it is important to determine whether the Bankruptcy Act does, in fact, purport to speak on the general subject of the effect of forfeiture clauses in leases in the event of bankruptcy or reorganization of a debtor. We find a definite expression of such a policy in section 70b of the Bankruptcy Act. That section contains a provision to the effect that:

> "A general covenant or condition in a lease that it shall not be assigned shall not be construed to prevent the trustee from assuming the same at his election and subsequently assigning the same; but an express covenant that an assignment by operation of law or the bankruptcy of a specified party thereto or of either party shall terminate the lease or give the other party an election to terminate the same shall be enforcible."

The policy represented by this provision of the statute can be better understood if read in the light of the decision of this Court in *Gaelay* v. *Williams, Trustee, etc.*, 210 U. S. 41. In that case the question was whether the bankruptcy of a tenant operated to terminate a lease which provided for its forfeiture "if said lessee shall assign this lease or underlet said premises, or any part thereof, or if said lessee's interest therein shall be sold under execution or other legal process, without the written consent of said lessors." The Court held that the bankruptcy did not forfeit the lease, that it passed to the trustee in bankruptcy, and that the latter had the right to assign the lease to a third party, despite the prohibition against assignment by the lessee. This policy enunciated by the Supreme Court in the *Gaelay* case of applying a most strict construction in order to prevent a for-

feiture which would deprive the bankrupt's creditors of a valuable asset, was codified in 1938 in the above quoted provision in section 70b of the Bankruptcy Act.

The policy of the Bankruptcy Law does not go so far as to state that forfeiture clauses of this character are invalid if the instrument in question enunciates the precise contingency of forfeiture *in unmistakable terms.* If, however, the expression of the forfeiture clause is equivocal or if the scope of its application is subject to doubt, the policy as stated by the statute and by this Court itself in the *Gaslay* case requires a construction that would obviate forfeiture.

The existence of this policy is recognized by the text writers on Bankruptcy. Thus, in 4 Collier on Bankruptcy (14th Edition, 1942), the authors in discussing section 70b of the Bankruptcy Act, state (pp. 1240, 1241) as follows:

> "Partly because of the general disinclination of courts to support penalties and forfeitures, and partly in order to allow the trustee to make the most of any valuable asset he may find in the estate, ambiguous contractual clauses and covenants in leases referring to forfeiture of the lease with respect to the lessee's bankruptcy have universally been construed in favor of the lessee and his estate. It may even be said that for the lessee's or his trustee's benefit ambiguities have sometimes been read into a lease which the naked eye was at a loss to discover. This form of benign interpretation has been consistently indulged in when the courts were faced with general clauses or covenants forbidding or restricting an assignment of the lease. The rule that such a clause or covenant does not prevent the trustee from selling or assigning the lease or sub-letting the premises is of old standing, and it is now explicitly sanctioned by the Act itself. Section 70b distinguishes between a 'general covenant or condition' that a lease shall not be assigned, on the one hand, and, on

the other, an 'express covenant' that an assignment by operation of law or the bankruptcy of a specified party or of either party shall terminate the lease or give the other party an election to terminate. The former shall not be construed to prevent the trustee from assuming and assigning the lease. The latter, however, shall be recognized and enforced. The practical upshot of this distinction is a restatement and clarification of the warning to draftsmen that has for many decades been deduced from case law and which may be thus formulated: The law does not inquire what the parties actually meant and intended by a forfeiture clause in connection with the assignment of a lease; it requires a kind of sacred and inflexible formula, much in the manner of the *stricti juris* formulae of pre-classical Roman law. It is not enough to say that a lease shall terminate or may be terminated if assigned to anyone—that is too 'general'. It must be said that the lease shall terminate or may be terminated upon assignment by operation of law, or, still more specifically, that it shall terminate or may be terminated upon the bankruptcy of the lessee (or the lessor or both)—that is 'express' enough."

It is not necessary to go as far as the above quotation seems to indicate, in order to hold that the forfeiture clause in the present lease is not invoked by the appointment of a trustee in reorganization proceedings under Chapter X. But it is unquestionably true that a forfeiture provision must be explicit and unequivocal in its application in order to invoke it. In the present case, as we will show, not only is the clause ambiguous in so far as the words "adjudged • • • insolvent" are claimed to apply to proceedings under Chapter X, but a reasonable interpretation thereof leads to the conclusion that "insolvent" is used in the bankruptcy sense.

The policy of strict construction of forfeiture clauses in the case of ordinary bankruptcy is even stronger where

reorganizations under Chapter X are involved. Chapter X was enacted by Congress to provide a more satisfactory method for the reorganization of corporations which found themselves in temporary financial straits. Its purpose was to permit the business of such corporations to be continued and their assets preserved for creditors and stockholders, rather than have them partially or wholly destroyed by proceedings in bankruptcy or equity receiverships. In innumerable instances, corporate contracts, including leases, constitute assets which, in many cases, are vital to the continuance of the business. Many such corporate contracts contain clauses of the type involved herein. If the decision in the instant case of the Circuit Court of Appeals for the Second Circuit should in such situations be followed, the very filing and approval of the petition for reorganization would immediately operate to cancel such executory contracts and thus defeat in large part the very purpose of the reorganization proceedings, inasmuch as every voluntary petition for corporate reorganization must allege under Section 130 of the Act that the corporation is "insolvent *or that it is unable to meet its debts as they mature.*"

In the light of the foregoing discussion, it seems clear that under the principle announced in *Prudence Realization Corp.* v. *Geist, Trustee, supra*, the federal law is applicable. In that case, this Court refused to apply the New York rule that "a guarantor of mortgage certificates who also has an interest in the mortgage cannot share in the proceeds of its collection until the certificate holders are paid unless there is a clear reservation in the certificate of the right of the guarantor to share on a parity with other certificate holders." The Court applied the rule and policy, set forth in the Bankruptcy Law, of equality to all creditors. The Court said (p. 95):

> "But so far as the New York cases, without evidence of the actual intent of the parties, subordinate the guarantor on grounds of 'presumed intention' or

'the existence of special equities' or the 'natural equities' involved (citing cases), we are unable to say that the rule laid down is other than one of State law governing the relative rights of claimants in a State liquidation. Nothing decided in Erie Railway Company *v.* Tompkins, 304 U. S. 64, requires a Court of Bankruptcy to apply such a local rule governing the liquidation of insolvent estates. The Bankruptcy Act prescribes its own criteria for distribution to creditors. In the interpretation and application of Federal Statutes federal not local law applies (citing cases). The Court of Bankruptcy is a court of equity to which the judicial administration of the bankrupt's estate is committed, Securities & Exchange Commission *v.* U. S. Realty Co., 310 U. S. 434, 455-475, and it is for that Court—not without appropriate regard to rights acquired under rules of state law, to define and apply federal law in determining the extent to which the inequitable conduct of a claimant in acquiring or asserting his claim in bankruptcy requires its subordination to other claims which, in other respects, are of the same class."

It is to be noted that in the *Prudence* case, the New York law recognized that an *explicit* statement in a mortgage certificate giving the guarantor a right to share equally with other certificate holders would be given effect; but the State policy refused to recognize equality or to interpret the certificate in such a way as to grant equality, in the absence of express and unmistakable language. The converse situation is true in the present case. It is the Federal law in the case at bar which, both by statute and by this Court's decisions, refuses as a matter of policy to recognize a forfeiture clause operating to deprive creditors of assets of the debtor, *unless the application of the invoked forfeiture clause expressly and unmistakably set forth.* In the *Prudence* case, the state

policy of strict construction gave way to the Federal policy of equality in distribution; in the instant case, the Federal policy of strict construction must likewise prevail; in fact, this policy, as we shall show, is in accord with the applicable State rule.

It should be remarked that neither this Court in the *Gazlay* case nor the Bankruptcy Act appears to have gone so far as to say that parties *cannot* provide that the contingency of bankruptcy or insolvency may operate to cancel a lease; they have clearly indicated, however, that the policy against forfeiture and against depriving creditors of a debtor's assets is so strong that explicit and unequivocal words must be used effectively to express any such intent. The policy of applying the Federal law in the present case would seem to be particularly clear in view of the fact that the institution of a proceeding under Chapter X—which is primarily designed to protect and conserve the debtor's assets, is seized upon as the ground for forfeiture of the lease and thus destroying what the statute was intended to conserve.

The decision in *Simmons* v. *National Tool Co.*, 110 Fed. (2d) 850, by the Circuit Court of Appeals for the Sixth Circuit, is directly in point, and in conflict with the decision herein by the Court below. In that case the National Tool Co. had a license under a patent to use certain grinding machines. The license contained a provision that "in the event of the bankruptcy, *insolvency* or dissolution of the National Tool Co., no title to said machines shall be vested in any receiver or trustee * * *" (italics ours). The National Tool Co. filed a petition for relief under Section 77B of the Bankruptcy Act in which it alleged that "the Debtor is unable to meet its debts as they mature* * *". The patentee contended that the filing and approval of the petition constituted an adjudication of insolvency of the National Tool Co. which operated as a cancellation or termination of the license. This is precisely the same claim which was made by the landlord in

the instant case. The Court flatly rejected this contention, stating, at page 850:

> "• • • it being the view of the court that the reorganization under Section 77B does not involve 'bankruptcy, insolvency or dissolution' in the sense those terms are used in the license agreement."

An examination of the record in the *Simmons* case discloses that the appellant in that case relied upon the cases in the Second Circuit of *In re Wil-Low Cafeterias, Inc.*, 95 Fed. (2d) 306 and *In re Walker*, 93 Fed. (2d) 281, which are the primary cases relied upon by the Circuit Court of Appeals for the Second Circuit in the case at bar. The Sixth Circuit obviously rejected the authority of said cases.

We proceed to inquire, therefore, whether the forfeiture clause here involved so explicitly and unmistakably applies to the proceeding under Chapter X as to necessitate the disregard of the policy above discussed.

POINT II

The term "insolvent" as used in the lease refers to insolvency in the bankruptcy sense.

Wholly apart from any question of policy as above discussed, and pursuing ordinary principles of construction, it seems clear that the word "insolvent", as used in the forfeiture clause, means excess of liabilities over assets rather than inability to meet obligations as they mature; and that the appointment of the trustee in the reorganization proceeding was *not* an adjudication of insolvency in the sense that this word is used in the lease.

It should be noted, preliminarily, that section 130 of the Bankruptcy Act setting forth the requisite allegations of a petition under Chapter X, says that "Every petition

shall state—(1) that the corporation is insolvent *or* unable to pay its debts as they mature." (Italics ours.) Clearly the words "unable to pay its debts as they mature" mean something other than insolvent; and it is undisputed that the Debtor is not "insolvent" in the sense that the word is used in the statute. Obviously, therefore, from the point of view of Chapter X itself, the granting of the petition for reorganization on the ground that the Debtor was unable to meet its debts as they mature, did not constitute an adjudication that the Debtor was "insolvent".

It is fundamental, moreover, that the clause of the lease in question *provides for a forfeiture,* that, wholly apart from the special policy discussed in Point I, forfeitures are not favored by the law, that provisions therefor will be strictly construed, and that all doubts must be resolved against the lessor. As Judge Learned Hand said in *Model Dairy Co., Inc.* v. *Foltis-Fischer, Inc.,* 67 Fed. (2d) 704, "It is true that courts do not look upon such conditions with a friendly eye, classing them as forfeitures," (citing cases).

The same principle of strict construction has been applied by the Court of Appeals of the State of New York in *Francis* v. *Ferguson,* 246 N. Y. 516. There the Court stated in part:

> "An ordinary covenant against assignment does not bind the executors of the tenant, and is not broken by a transfer of the leased premises by operation of law, Squire *v.* Learned, 196 Mass. 134; 81 N. E. 880; 11 L. R. A. (N. S.) 634, 124 Am. St. Rep. 525, 12 Ann. Cas. 977; Gazlay *v.* Williams, 210 U. S. 41, 28 S. Ct. 687, 52 L. Ed. 950. The covenant may, however, be so drawn as expressly to prohibit such a transfer. To accomplish such a prohibition in case of a devolution to executors, *its language must be 'very special'.* Seers *v.* Hind, 1 Ves. Jr. 294. *Such covenants are construed 'with the utmost jealousy'.* Higgs *v.* Pursell, 66 N. Y. 193, 201." (Italics ours.)

Professor Williston states the rule simply:

> "Therefore construction of a contract which would lead to a forfeiture cannot be favored." (3 Williston on Contracts (1936) Sec. 620, p. 1787.)

With this fundamental principle in mind, we proceed to the construction of the word "insolvent" as used in the lease. For convenience, we repeat the pertinent words in paragraph 4 of the lease (R. 5):

> "• • • if a petition in bankruptcy shall be filed by the tenant or if the tenant shall be adjudged bankrupt or insolvent by any Court, or if a trustee in bankruptcy of the tenant shall be appointed in any suit or proceeding brought by or against the tenant, then in each and every such case, the term hereby granted shall immediately cease, determine and come to an end • • •".

It is the petitioner's contention that the entire provision refers, in different ways, merely *to different forms of an ordinary bankruptcy proceeding;* and that "insolvent" is used in the bankruptcy sense of greater liabilities than assets.

The first clause of said provision—"if a petition in bankruptcy shall be filed by the tenant", refers to a *voluntary* bankruptcy proceeding. Then follows the second clause: "or if the tenant shall be adjudged bankrupt or insolvent by any Court". This, it would seem, reasonably applies to *involuntary* proceedings in bankruptcy resulting in an adjudication. The next phrase reads: "or if a trustee in bankruptcy of the tenant shall be appointed in any suit or proceeding brought by or against the tenant". Again we see that the parties in this provision concerned themselves just with bankruptcy proceedings—in this instance, the actual appointment of a trustee in bank-

ruptcy, whether the proceedings were voluntary or involuntary.

We accordingly have an elaborately phrased, but entirely consistent scheme, which concerns itself solely with bankruptcy, whether voluntary or involuntary. The intent was protection of the landlord against bankruptcy proceedings; it follows that the terms "bankrupt" and "insolvent" are used interchangeably.

The rule of *"ejusdem generis"* strongly supports our view. The word is used in the same phrase with "bankrupt" and is both preceded and followed by language which unmistakably refers solely to bankruptcy. The application of the *"ejusdem generis"* rule is clearly called for.

In view of the sedulousness which the lessor used in encompassing every phase of bankruptcy proceedings, the failure to mention other possible financial difficulties of the tenant indicates clearly that such other situations were not contemplated by this clause. There is no provision, for example, that the appointment of a receiver constitutes a ground of forfeiture, notwithstanding the frequency with which equity receivership proceedings were at that time resorted to. Nor is there any provision, quite common in leases, requiring the tenant to vacate any levy or attachment against its property. Nor does the lease declare that an assignment for the benefit of creditors shall be ground for forfeiture. In this respect the lease in question differs from those involved in *In re Wil-Low Cafeterias, Inc.*, 22 F. Supp. 617; *In re Walker*, 93 F. (2d) 281, and *Model Dairy Co., Inc.* v. *Foltis-Fischer, Inc.*, 67 F. (2d) 704—all in the Second Circuit. The Court below itself recognized this distinction, saying (R. 45): "It is true, as appellant urges, that in these cases the forfeiture clauses were more detailed than is the clause now under consideration; and it is likewise true, as was said in the *Model Dairy* opinion, *supra*, that such clauses are not viewed with 'a friendly eye'."

It is difficult to believe that a landlord who in the present case so meticulously sought to protect himself against the particular contingency of bankruptcy would have been so slip-shod and careless with respect to other contingencies if he had intended that they, likewise, should effect a forfeiture.

The Circuit Court of Appeals recognized the applicability of the rule that clauses providing for forfeitures must be strictly construed, but was of the opinion that its decision was necessitated in order to give "meaning to every word the parties use"; and that the construction for which petitioner contends "would deprive the words 'or insolvent by any court' of all utility; they would add nothing to the preceding words 'adjudged bankrupt'" (R. 45). This contention, as we shall show, contains a double fallacy.

In the first place, by applying the rule of *ejusdem generis*, it has been frequently held that several words may be used to convey a similar meaning. Indeed, in the very clause in question as above quoted, the parties stated that upon the happening of any of the grounds of forfeiture, "the term hereby granted shall immediately *cease, determine, and come to an end.*" Can it be seriously urged that separate meanings are to be attached to the respective words "cease", "determine" and "come to an end"? Moreover, the clause "if a trustee in bankruptcy of the tenant shall be appointed in any suit or proceeding brought by or against the tenant" is entirely unnecessary in view of the preceding phrases covering the contingency of the filing of a voluntary petition in bankruptcy by the tenant and the contingency "if the tenant shall be adjudged bankrupt or insolvent by any Court". In the very clause under consideration, therefore, we find several instances of the use of repetitious phrases merely for emphasis or excess of caution.

Our construction has, moreover, a sound practical basis. A landlord, reasonably enough, may not wish to be bound

to a lease with a bankrupt tenant. The very fact of bankruptcy means not only that the debts will not be paid in full, but that the debtor's business *will be liquidated.* The sooner the landlord obtains possession of the premises under these circumstances, the better off he will be. This is by no means true in the event of insolvency in the equitable sense. The debtor is likely to emerge from an equity receivership or a reorganization proceeding under Chapter X in stronger financial condition than before. The lease being assumed, the landlord is assured his full rent.

This argument is even stronger in the lease under consideration, where the very happening of the events of default expressly constitutes an *automatic cancellation of the lease.* If the rental value of premises covered by such a lease should substantially decrease, the landlord would have an advantageous lease terminated, and a fundamentally desirable tenant lost, irrespective of whether or not he desired it. It is difficult to believe that the landlord intended such a result.

The second fallacy in the reasoning of the Circuit Court of Appeals will be discussed in the next point.

POINT III

Assuming, arguendo, that the words "adjudged * * * insolvent" are to be construed as not relating to bankruptcy proceedings, then they should reasonably be construed to refer to an adjudication of insolvency under the New York Insolvency Law as set forth in the Debtor and Creditor Law of that State.

The Circuit Court of Appeals, as we have seen, based its decision upon the theory that in the phrase "adjudged bankrupt or insolvent by any Court", the word "insolvent" must be given a distinct meaning from that attached to "bankrupt". It thereupon concluded that "insolvent"

meant inability to meet debts as they mature. Even assuming, however, that the premise is correct, the conclusion by no means follows. If the two words are not intended to comprehend the same situation, then an obvious and reasonable purpose existed for the use of the word "insolvent" in addition to "bankrupt". The Federal courts, of course, have exclusive jurisdiction over bankruptcies in the administration of the National Bankruptcy Act. On the other hand, if, as has several times occurred in our history, no National Bankruptcy Act is in existence, then the respective State laws covering insolvencies are applicable. The State of New York has such an insolvency law. It is contained in sections 50 to 88, inclusive, of the New York Debtor and Creditor Law. This law has not been repealed by the enactment of the National Bankruptcy Act; it is merely suspended in operation.

Stellwagen v. *Clum*, 245 U. S. 605, 613.

Prior to 1898, the federal bankruptcy laws were short-lived and widely spaced in time. The Act of 1800 was repealed in 1803. The next legislation, enacted in 1841, was repealed in 1843. The Act of 1867 was repealed in 1878. (1 Collier on Bankruptcy, 14th Edition, pages 7-9.)

An entirely reasonable and understandable purpose of the language under consideration was to provide that an adjudication of *insolvency* under the State insolvency law should constitute a forfeiture during any period that the National Bankruptcy Act was not in existence. Debtors under the National Bankruptcy Act are adjudicated "bankrupt"; under the State insolvency law they are adjudicated "*insolvent*". The State insolvency law does not use the word "bankrupt". The words "adjudged • • • insolvent by any Court" would afford the landlord protection during any gaps when no national bankruptcy act was in force. It would seem clear, therefore, that if any separate purpose is to be attached to "or insolvent", that purpose was to cover the contingency of proceedings

under the New York insolvency law as set forth in the Debtor and Creditor Law. Obviously, there has been no adjudication under that law that the Debtor was insolvent.

It is of fundamental importance, moreover, to note that the definition of insolvency under the New York Debtor and Creditor Law is *not* inability to meet obligations as they mature, but an *insufficiency of assets to meet debts.* Thus, section 52 of that law, defining what a petition for an adjudication of insolvency must contain, states:

> "Sec. 52. *Contents of petition.*—The petition must be in writing; it must be signed by the *insolvent,* * * *; it must set forth, in substance, that *he is unable to pay all his debts in full;* * * *" (Italics ours).

We urge, therefore, that if any distinctive purpose were intended to be served by the use of the words "or insolvent" after "adjudged bankrupt", that reason was to cover the contingency of an adjudication of insolvency under the State insolvency law in the absence of a federal bankruptcy statute; that contingency has not occurred; and, indeed, the word "insolvent" as used in the State Statute *has precisely the same meaning as it has under the National Bankruptcy Act, namely, an insufficiency of assets to cover liabilities.*

POINT IV

To say the least, the meaning of "insolvent", as used in the clause in question, is ambiguous; accordingly, a construction should be adopted which would avoid a forfeiture of the lease.

An examination of the New York law discloses that in many instances, both under the Common Law and by Statute, insolvency has been defined in the sense of more liabilities than assets.

As we have seen, the Debtor and Creditor Law of that State, which in sections 50 to 88 thereof, sets forth a comprehensive insolvency law, defines an "insolvent" as one who is "unable to pay all his debts in full" (Section 52). Insolvency is similarly defined by the New York law in many other instances. Thus, in *Kane* v. *Larkin*, 131 N. Y. 300, 307, 308, the Court of Appeals of New York as early as 1892, long before the lease in question was made, stated (p. 307) in a case involving a fraudulent conveyance, that:

> "If the grantor remains insolvent after the conveyance and *has sufficient property left to satisfy all his debts*, then the conveyance, whatever his intention, cannot be a fraud upon his existing creditors." (Italics ours.)

And again:

> "But the person assailing the deed assumes the burden of showing that it was executed in bad faith and that it left the grantor insolvent *and without ample property to pay his existing debts and liabilities* and so it has been repeatedly held." (Italics ours.)

A similar definition of "insolvency" is contained in Article 10 of the Debtor and Creditor Law, dealing with fraudulent conveyances. Thus, section 271 states:

> "Insolvency. 1. A person is insolvent when the present fair salable value of his assets is less than the amount that will be required to pay his probable liability on his existing debts as they become absolute and matured."

It is true that this section was enacted in 1925, after the making of the lease in question, but, as we have seen, it is merely a codification of the New York common law definition of insolvency as set forth in *Kane* v. *Larkin, supra.*

So, too, section 101 of the Debtor and Creditor Law (contained in Article 4 of said law dealing with "Insol-

vent's Exemption from Arrest and Imprisonment), provides as follows:

> "Section 101. Contents of Petition.—The petition must be in writing; it must be signed by the *insolvent* * * * it must set forth in substance, that he is unable to pay all his debts in full; * * *"

In section 955 of the Penal Law of the State of New York, which deals with "Transactions by Brokers and Dealers after Insolvency", insolvent is defined as follows:

> "Any person, firm, association or corporation shall be deemed insolvent within the meaning of this section whenever the aggregate of his or its property shall not, at a fair valuation, be sufficient in amount to pay his or its debts."

It would seem that these definitions of insolvency in New York, particularly in the Debtor and Creditor Law which purports to define the respective rights between parties in the relationship indicated by the title, would be most persuasive as to the meaning of the parties. *To say the very least, there is an ambiguity.* That being the case, since a forfeiture is involved, the ambiguity should be resolved in favor of the tenant.

CONCLUSION

It is respectfully submitted that the decision herein of the Circuit Court of Appeals for the Second Circuit should be reversed.

Dated April 5, 1945.

JOSEPH LORENZ
Counsel for the Petitioner.

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Supreme Court of the United States

OCTOBER TERM, 1944 No. 953

IN THE MATTER

OF

CHILDS COMPANY,
Debtor.

IN PROCEEDINGS FOR REORGANIZATION UNDER CHAPTER X OF THE BANKRUPTCY ACT.

No. 82,868.

JOHN F. X. FINN, as Trustee of Childs Company,
Petitioner,

v.

BURTON C. MEIGHAN, JR., as Substituted Trustee under the Last Will and Testament of WILLIAM T. WOOD, Deceased,
Respondent.

BRIEF OF RESPONDENT OPPOSING PETITION FOR WRIT OF CERTIORARI

BURTON C. MEIGHAN, JR.,
Counsel for Respondent.

MEIGHAN & NECARSULMER, Esqs.,
Attorneys for Respondent.

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BRIEF OF RESPONDENT OPPOSING PETITION FOR WRIT OF CERTIORARI

To the Honorable the Chief Justice and Associate Justices of the Supreme Court of the United States:

I. Opinions Below

The opinion of the Circuit Court of Appeals (per Swan, C.J.) appears in the Record at pages 63-65 and

has not as yet been officially reported. The opinion of the District Court is found in the Record at pages 51-55 and has not as yet been officially reported.

II. Statement of Case

The respondent makes no objection to the statement of the case in the petition.

The sole issue before the Circuit Court of Appeals for the Second Circuit concerned the correctness of the District Court in construing the clause, "if the tenant shall be adjudged bankrupt or insolvent by any court" to apply to the order of the bankruptcy court approving the petition of Childs Company in reorganization and appointing a trustee.

This case does not present any question falling within the category of those defined in Rule 38 of this court as appropriate for certiorari.

The conflict, alleged by petitioner to exist between the Second Circuit and the Sixth Circuit, is illusory and nonexistent.

Everyone of the specifications of error (Brief of Petitioner, p. 6) states an erroneous interpretation of the lease relating to cancellation.

A decision by this court would be of no value as a precedent except in cases involving leases with precisely the same covenants and the same facts.

III. Argument

(A) The decision of the Circuit Court of Appeals for the Sixth Circuit reported in 110 Fed. (2nd) 850 is not in conflict with the decision of the Circuit Court of Appeals for the Second Circuit in the instant matter (not as yet officially reported) set forth in Record at pages 63, 65.

To support a real or true conflict between circuits there must exist comparability of issues. That situation does not exist here.

The sole issue of law involved in this matter (forfeiture of lease) is not the same as that which was before the Sixth Circuit in the *Simmons* case. In that case the issue was the right to maintain an equity suit for damages and profits by reason of an alleged patent infringement. *No forfeiture of a lease or other contract was involved.*

The license agreement, after declaring National Tool Company to be the sole owner of six grinding machines, built at its own expense, with the right to use said machines in its factory at Cleveland, Ohio, states, "but the National Tool Company shall not have the right to sell or dispose of said machines directly or indirectly to any person or persons whatever, and in the event of the bankruptcy, insolvency or dissolution of the National Tool Company no title to said machines *shall be vested in any receiver or trustee for purposes of using them in gear grinding shaper cutters*." (Italics supplied.)

There was nothing in the license to prevent the National Tool Company, the licensee, from using the machines even while involved in bankruptcy, insolvency or dissolution proceedings, or after its emergence from

any such proceedings. The license agreement did not provide for forfeiture—*it simply prohibited the sale of the machines to another or the passage of title from the licensee to any trustee or receiver.*

In the instant case the court below had before it a long-term lease containing a definite and unequivocal forfeiture clause for the purpose of determining the scope of the said forfeiture clause.

The license agreement in the *Simmons* case and the forfeiture clause in the instant matter are not at all comparable, and a decision involving the intent of the parties in one is of no pertinency to the intent of the parties in the other.

Petitioner is manifestly in error in attempting to support his contention of conflict by inferring that the Circuit Court in the *Simmons* case passed upon a *forfeiture* issue or that the appeal from the District Court decision involved that issue. Counsel for Simmons, in the course of argument before the District Court, stated: "Nowhere in the bill of complaint was it alleged that the old National Tool Company *had forfeited its rights under the license agreement in question.*" (Italics supplied.) The District Court (opinion not officially reported) stated: "No forfeiture is prayed for. * * *"

The record in the *Simmons* case further indicates that Simmons and her counsel did not petition the bankruptcy court, pending reorganization proceedings, to declare a forfeiture of the license agreement, nor did they file any objections or take any exceptions to the reorganization proceedings. It should also be noted that the decree of confirmation provided, "that the status of the executory contracts of the debtor described in these proceedings and the rights, privileges and liabilities of the

parties herein with respect thereto, as now existing, *shall not be altered, impaired or affected by these proceedings*". (Italics supplied.)

The basis for the Simmons decision was estoppel. As the District Court so aptly put it:

> "The question of the debtor's right to continue under the contract should have been fought out before the master recommended, and the bankruptcy judge approved and confirmed, the plan of reorganization which continued the contract in force and unaffected by reorganization. • • •
>
> "Plaintiff took no action whatever in the 77-B proceedings of the debtor and took no exceptions and made no objections to the findings and report of the Special Master, or to the entering of the decree of confirmation."

An examination of the Simmons record indicates that any other decision by the District Court or by the Circuit Court of Appeals *would have permitted Simmons to attack collaterally the concluded bankruptcy proceedings.*

The Second Circuit decisions (*In re Walker*, 93 Fed. (2nd) 281; *In re Wil-low Cafeterias*, 22 Fed. (Supp.) 617, rev'd on another ground 95 Fed. (2nd) 306, cert. den. 304 U. S. 567) referred to by Simmons in her appeal brief were not considered by the Sixth Circuit since they were not pertinent to the issue in that case. The opinion of the Sixth Circuit does not discuss or even mention these cases.

Petitioner has assumed a conflict, when, in fact, none exists, by fragmentary references to the Simmons brief and record.

(B) The filing, and the approval by the District Court, of the petition by Childs Company for reorganization under Chapter X of the Bankruptcy Act terminated the lease pursuant to and by virtue of the forfeiture provisions contained in said lease.

The approval of the petition by the debtor by the District Court below constituted an adjudication of insolvency in that the said debtor was unable to pay its debts as they matured. *In re Walker*, 93 Fed. (2nd) 281, U.S.C.A. §§530, 541 (Title 11).

It should be noted that this lease is a New York contract made in 1922. New York definitions of insolvency prevailing in 1922 do serve to demonstrate the interpretations and meanings of the word insolvency existing at the time the said lease was drawn. For example, the term insolvency used in the Stock Corporation Law (Section 15) has always connoted inability to meet obligations as they mature (*French* v. *Andrews*, 81 Hun 272, aff'd 145 N. Y. 441). Again, the provision in the General Corporation Law providing for dissolution where the corporation has remained insolvent for at least one year (Section 71) contemplates a failure to pay debts as they mature (*Denike* v. *New York Lime and Cement Company*, 80 N. Y. 599). A further example appears in the definition of the word insolvency in Section 156, Subdivision 3, of the Personal Property Law. Furthermore, in the absence of statute, the term has come to mean inability to meet obligations as they mature (*Sterrett* v. *Third National Bank*, 46 Hun 22, aff'd 122 N. Y. 659; *Hood* v. *Guaranty Trust Co.*, 270 N. Y. 17, 24).

Petitioner argued below that the definition of insolvency in New York Debtor-Creditor Law, enacted in

1925, should be read into the lease. This contention was rejected by the court below. The decision below is not contrary to any New York decision. *Kane* v. *Larkin*, cited by petitioner, involved an attempt to set aside a preferential transfer and not the construction of a lease or other contract. The Debtor-Creditor Law is limited to cases involving conveyances in fraud of creditors and does not represent a general New York definition of insolvency (*Wilcox* v. *Goess*, 16 Fed. (Supp.) 350).

This court has said in *Thompson* v. *Consolidated Gas Co.*, 300 U. S. 55, 74, that:

> "When not instructed by some decision of a state court, we are disposed * * * to accept the construction given by the lower federal court to a statute of the State, particularly when that court is composed, as in this instance, wholly of citizens of the State, familiar with the history of the statute, the local conditions to which it applies, and the character of the State's laws."

Reliance upon New York statutes is not necessary, however, the court below having expressed itself on similar lease clauses drawn about the time of the instant lease in holding the word "insolvency" to mean an inability to meet obligations as they mature and not insolvency in the bankruptcy sense (*In re Willow Cafeterias*, 95 Fed. (2nd) 306, cert. den. 304 U. S. 567; *In re Walker*, 93 Fed. (2nd) 281).

The contention of petitioner (Petitioner's Brief, 1st paragraph, p. 13) that "insolvent" as used in the forfeiture clause of the lease refers to insolvency in the bankruptcy sense was rejected by the court below. As stated by Judge Swan (Record, p. 65):

> "But such a construction would deprive the words 'or insolvent by any court' of all utility; they would add nothing to the preceding words 'adjudged bankrupt'. * * * Since the time-honored meaning of insolvency, in the absence of a statute specifying another meaning, is inability to meet obligations as they mature in ordinary course of business, it is entirely reasonable to suppose that the parties used 'insolvent' in that sense rather than in the limited sense already covered by 'adjudged bankrupt'."

Petitioner argues under Point II (Brief of Petitioner, pp. 9-10) that the decision of the court below tends to defeat the very purpose of reorganization proceedings, and that the question is novel.

This very argument was made by counsel for the debtor in the *Wil-low Cafeterias* case when petitioning this court for a writ of certiorari. The petition in that case was denied (*In re Wil-low Cafeterias*, 304 U. S. 567, case #967, October term, 1937).

The question presented by petitioner is not novel and requires no decision by this court. The question is not what constitutes insolvency as that word is used in the Bankruptcy Act or in state statutes but as to the sense in which the word insolvent was used in this particular contract. As stated by Judge Patterson in the *Wil-low Cafeterias* case:

> "It is idle to discuss the policy behind the enactment of Section 77-B, the question being not what the word 'insolvent' meant to Congress in passing the act but what it meant to the lessor and the lessee when they wrote it into these leases."

Such question is not one deserving the attention of this court.

IV. Conclusion

Involving as it does only the interpretation of a lease, consideration of state laws and the special facts of this case, and without any substantial reason to believe that error has occurred or that injustice has been done, the petition for a writ of certiorari should be denied.

Respectfully submitted,

BURTON C. MEIGHAN, JR.,
Counsel for Respondent.

LOUIS A. MARCHISIO,
Of Counsel.

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Supreme Court of the United States

OCTOBER TERM, 1944

No. 953

JOHN F. X. FINN, as Trustee of Childs Company,
Petitioner,

v.

BURTON C. MEIGHAN, JR., as Substituted Trustee under the Last Will and Testament of WILLIAM T. WOOD, Deceased,
Respondent.

BRIEF OF RESPONDENT

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Supreme Court of the United States

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JOHN F. X. FINN, as Trustee of Childs Company,
Petitioner,

v.

BURTON C. MEIGHAN, JR., as Substituted Trustee under the Last Will and Testament of WILLIAM T. WOOD, Deceased,
Respondent.

BRIEF OF RESPONDENT

Opinions Below

The opinion of the Circuit Court of Appeals for the Second Circuit is officially reported in 146 Fed. (2d) 594 (R. 43-45). The opinion of the District Court is set out in the Record at pages 36-39 and has not as yet been officially reported.

Jurisdiction

Writ of Certiorari was granted on March 5th, 1945 (R. 47).

The order allowing certiorari contained a request that counsel discuss in their briefs and upon oral argument the question whether the construction of the contract is governed by federal or state law.

Statement of Case

The respondent makes no objection to the statement of the case set out in the petitioner's brief on the merits.

The issue before this Court can be briefly stated as follows:

> The petitioner seeks a reversal of the decision of the Circuit Court of Appeals for the Second Circuit, affirming the action of the United States District Court for the Southern District of New York, in construing the clause "if the tenant shall be adjudged bankrupt or insolvent by any court" to apply to the order of the bankruptcy court which approved the petition of Childs Company for reorganization under Chapter X of the Bankruptcy Act and appointing John F. X. Finn as Trustee.

Summary of Argument

The construction of the forfeiture clause in the lease, in the absence of federal legislation, is governed by state and not federal law. Since the provisions of the bankruptcy laws are silent as to the construction to be placed upon the word "insolvent" as used in the clause "if the tenant be adjudged bankrupt or insolvent by any court" the federal courts must apply local law as evidenced by decisions of the state.

Both state and federal law have construed the word "insolvent" as used in the forfeiture clause to mean inability to meet obligations as they mature in the ordinary course of business and not in the bankruptcy sense of excess of liabilities over assets. Since state and federal law are in accord, it is unnecessary for this court to determine whether state or federal law applies.

The decision of the courts below construed the word "insolvent" so as to give effect to the fair meaning of the language as used by the draftsman of the lease and no statute or principle of law requires a construction of the word in the limited bankruptcy sense of excess of liabilities over assets.

The case of *Simmons* v. *National Tool Company*, 110 Fed. (2nd) 850 (C.C.A. 6), is not in conflict with the decision of the court below. The basis for the decision in the *Simmons* case was estoppel. Accordingly, the word "insolvent" and the interpretation to be placed thereon was not involved and was not considered by that court.

POINT I

The construction of the forfeiture clause in the lease, in the absence of federal legislation, is governed by state and not federal law.

State law, in determining the substantive rights of parties to a contract, is controlling in connection with a bankruptcy matter insofar as it does not conflict with any bankruptcy provision passed by Congress in the exercise of its constitutional power (*United States* v. *Bethlehem Steel Corporation*, 315 U. S. 289). In the event of a conflict the provision of the Bankruptcy Act will accordingly prevail and is to be applied by the federal courts sitting as a court of bankruptcy (*Sola Electric Company* v. *Jefferson*, 317 U. S. 173).

In the instant case, since the provisions of the bankruptcy laws are silent as to the construction to be placed on the word "insolvent", local and not federal law applies (*Erie Railroad Company* v. *Tompkins*, 304 U. S. 64). As was said in *Meredith* v. *Winter Haven*, 320 U. S. 228

> "Erie v. Tompkins did not free the federal court from the duty of deciding questions of state law in diversity cases. Instead, it placed on them a greater responsibility for determining and applying state law in all cases *within their jurisdiction in which federal law does not govern.*" (Italics ours).

Again, in *D'Oench, Duhme & Company* v. *Federal Deposit Insurance Company*, 315 U. S. 447 (concurring opinion by Mr. Justice Frankfurter):

> "There is no federal statute to override either the Missouri law as to estoppel or the Illinois law which treats respondent as a holder in due course. Were this court, in the absence of federal legislation, to make its own choice of law, Illinois or Missouri law would furnish the governing principles."

Counsel for petitioner contends that because of Section 70-b of the Bankruptcy Act (11 U.S.C.A., Section 110) federal, and not state law, is to apply in connection with the construction to be placed upon the word "insolvent" as used in the forfeiture clause in the lease. Petitioner overlooks the fact that this section goes no further than to establish a rule of construction to be placed upon covenants against assignments as expressed by this Court in *Gazlay* v. *Williams, Trustee*, 210 U. S. 41, which rule of law is in agreement with state rules (*Francis* v. *Ferguson*, 246 N. Y. 516). Furthermore, section 70-b does not void forfeitures but, on the contrary, it expressly permits them. It has not changed the law as to construction of leases nor the proposition that local law will be followed unless it is in conflict with a constitutional provision passed by Congress (*Erie* v. *Tompkins, supra*; *United States* v. *Bethlehem Steel Corporation, supra*).

POINT II

Both state and federal law construe the word "insolvent" as used in the forfeiture clause to mean inability to meet obligations as they mature in the ordinary course of business.

The primary issue in this case is whether the clause "if the tenant shall be adjudged bankrupt or insolvent by any court" applies to the order of the bankruptcy court which approved the petition of Childs Company for reorganization.

On October 26, 1943, the debtor filed a petition praying for relief under the Chandler Act, in which petition the debtor stated that it was unable to pay its debts as they mature. The District Court entered an order approving the petition as filed. This is an adjudication that the debtor is unable to pay its debts as they mature. Section 141 of the Bankruptcy Act (11 U.S.C.A., Section 541); Section 131 of the Bankruptcy Act (11 U.S.C.A., Section 530); *In re Walker*, 93 Fed. (2nd) 281 (C.C.A. 2).

Federal courts have construed the word "insolvent" to mean inability to meet debts as they mature in the ordinary course of business in forfeiture clauses similar to the one in the instant case (*In Schulte Retail Stores*, 22 Fed. Supp. 612, aff'd *In re Walker*, 93 Fed. (2) 281; *In re Wil-low Cafeterias, Inc.*, 22 Fed. Supp. 615, rev'd on another ground 95 Fed. (2) 306, cert. den. 304 U. S. 567). Judge Knox in the *Schulte* case said:

> "Obviously, the draughtsman of the lease did not intend that his alternatives should be construed as synonymous. If the phrase 'proceedings in bankruptcy' be interpreted strictly and most favor-

ably to the debtor, we may assume that it pertained to the condition of liabilities exceeding assets. Hence, 'insolvent' must be taken to apply to situations not precisely within the purview of a bankruptcy proceeding, as of the date of the lease, viz. 1920, and inability to meet obligations as they matured was just such a situation. Hence, I believe that the debtor has admitted insolvency within the forfeiture clause.

"This conclusion is buttressed by the legal definitions of insolvency prevailing at the time the lease was drawn. The word has been most frequently interpreted in connection with section 15 of the Stock Corporation Law, Consol. Laws, c. 59. The term insolvency in that statute has always connoted inability to meet obligations as they mature. Brouwer *v.* Harbeck, 9 N. Y. 589; Abrams *v.* Manhattan Brewing Company, 142 App. Div. 392; 126 N. Y. S. 844; French *v.* Andrews, 81 Hun 272; 30 N. Y. S. 796, affirmed 145 N. Y. 441, 40 N. E. 214. General Corporation Law, Consol. Laws, c. 23 §71, provides for dissolution 'where the corporation has remained insolvent for at least one year.' This section, upon the rare occasions when it has been invoked contemplates a failure to pay debts as they mature. People *v.* Troy Chemical Co., 118 App. Div. 437, 104 N. Y. S. 22. See, also, Benike *v.* New York Lime & Cement Company, 80 N. Y. 599. Another definition of insolvency is to be found in Personal Property Law, Consol. Laws, c. 41, §156, subd. 3.

"The foregoing statutes are obviously not controlling in the instant case, since they are used in connection with special situations, but they serve to demonstrate the interpretations and meaning of the term 'insolvency' existing at the time the lease was drawn. Furthermore, in the absence of statute, the term has come to mean inability to meet obligations as they mature. See Sterrett *v.* Third

National Bank, 46 Hun 22, affirmed 122 N. Y. 659, 25 N. E. 913; Brown *v.* Montgomery, 20 N. Y. 287, 75 Am. Dec. 404. Debtor and Creditor Law, Consol. Laws, c. 12, §271, upon which the debtor relies, was enacted in 1925, and has no bearing on the interpretation of a term in a lease made in 1920.

"I conclude that the debtor has admitted it is 'insolvent', as that term was used in the lease and in the light of its meaning under the law of New York."

Similarly, Judge Patterson in the *Wil-low Cafeterias* case:

"It is the meaning commonly attached to insolvency by the New York Courts, unless some other definition is demanded by statute. Brouwer *v.* Harbeck, 9 N. Y. 589; Denike *v.* New York & Rosendale Lime & Cement Co., 80 N. Y., 599; French *v.* Andrews, 81 Hun 272, 30 N. Y. S. 796, affirmed 145 N. Y. 441, 40 N. E. 214; Baker *v.* Emerson, 4 App. Div. 348, 38 N. Y. S. 576; Horrocks Desk Co. *v.* Fangel, 71 App. Div. 313, 75 N. Y. S. 967; Joseph *v.* Raff, 82 App. Div. 47, 81 N. Y. S. 546, affirmed 176 N. Y. 611, 68 N. E. 1118; Abrams *v.* Manhattan Consumers' Brewing Co., 142 App. Div. 392, 126 N. Y. S. 844. The leases in question, being leases made in New York and covering real estate in New York, the parties will be taken to have used the word 'insolvent' in the sense given it by the New York law and to have intended that the lessor might terminate the leases if the lessee should arrive at a condition in which it was unable to pay its debts in ordinary course as they matured. It is idle to discuss the policy behind the enactment of section 77b, the question being not what the word 'insolvent' meant to Congress in passing that act but what it meant to the lessor and the lessee when they wrote it into these leases. This conclu-

sion is in accord with the view of Judge Knox in re: Schulte Retail Stores Corporation, 22 F. Supp. 612, decided March 27, 1937."

Again, in the words of Judge Hand in the *Walker* case:

> "The insolvency mentioned in the lease cannot have been other than a failure to meet the lessee's obligations as they matured; that is the insolvency which throws the lessor's relations into confusion, delays payment of the rent, impounds his property for an indefinite time, and in general makes it important for him to be free to reenter."

The decisions of the State of New York are of the same tenor. In *American Castaye Corporation* v. *Niles-Bement-Pond Company*, 266 A. D. 557, the Appellate Division, First Department, of New York Supreme Court, had before it for construction the word "insolvency" in a cancellation clause in a licensing agreement reading as follows:

> "If the corporation becomes insolvent or bankrupt or goes into liquidation, the license hereby granted shall thereupon terminate, cease and become null and void."

It appeared from that case that the licensee corporation was unable to meet its debts as they matured in the ordinary course of business, and the question before the court was whether the word "insolvent" as used in the cancellation clause meant inability to meet obligations as they matured in the ordinary course of business. The Court stated:

> "Under our common law 'insolvency' means inability to meet obligations as they mature in the

> ordinary course of business. (Brower *v.* Harbeck, 9 N. Y. 589; Denike *v.* New York Lime & Cement Company, 80 N. Y. 599; Abrams *v.* Manhattan Consumers Brewery Company, 143 A. D. 392)".

While forfeiture clauses are to be strictly construed, nevertheless, they are valid and will be enforced. The construction to be placed upon such clauses must give effect to the fair meaning of the language used (Section 70b Bankruptcy Act, 11 U.S.C.A. Section 110; *Model Dairy, Inc. v. Foltis-Fisher, Inc.*, 67 Fed. (2) 704; *Gillette Bros.* v. *Aristocrat Restaurant*, 239 N. Y. 87). As Judge Learned Hand in the *Model Dairy* case phrased it:

> "It is true that courts do not look upon such conditions with a 'friendly eye', classing them as forfeitures. (Citing cases.) Nevertheless, they are valid and we must give effect to the fair meaning of the language used."

Or as was said by Judge Andrews in the *Gillette Bros.* case:

> "Working a forfeiture, the language is to be strictly construed. * * * The clause should be given a reasonable construction."

That the construction placed upon the word "insolvent" by the courts below is reasonable and gives effect to the meaning [redacted] INTENDED to be conveyed by the draftsman when writing the lease in 1927, is clearly indicated by the following statement in the opinion of Judge Swan:

> "The Appellant contends that 'insolvent' as used in paragraph 4 of the lease refers to insolvency in the bankruptcy sense, that is, to an excess of liabilities over assets, rather than a

> inability to meet obligations as they mature. But such a construction would deprive the words 'or insolvency by any court' of all utility; they would add nothing to the preceding words 'adjudged bankrupt' * * * since the time honored meaning of insolvency, in the absence of a specified other meaning, is inability to meet obligations as they mature in the ordinary course of a business, it is entirely reasonable to suppose that the parties used 'insolvency' in that sense, rather than in the limited sense already covered by 'adjudged bankrupt'."

From the foregoing it appears that both federal and state decisions are in accord when construing the word "insolvent" and a determination as to whether state or federal law applies in the instant case is not necessary (*D'Oench, Duhme & Company* v. *F.D.I.C.*, 315 U. S. 447 (concurring opinion of Mr. Justice Frankfurter); *Prudence Realization Corporation* v. *Ferris*, case 137—October Term, 1944, decided January 24, 1945 (concurring opinion of Mr. Chief Justice Stone). In the *Prudence* case, Mr. Chief Justice Stone stated:

> "[redacted] judgment should be affirmed, not because the plan called for determination [redacted] of petitioner's rights in bankruptcy by state, rather than federal law, but because in the circumstances of this case the applicable federal law is the same as that which the state court has applied".

Phrased by Mr. Justice Frankfurter in the *D'Oench* case:

> "The Chief Justice and I concur in the result on the ground that in the circumstances of this case respondent is entitled to recover whatever law is deemed controlling."

POINT III

No statute or principle of law requires a construction of the word "insolvent" in the bankruptcy sense of excess of liabilities over assets.

Petitioner stresses the definition of insolvency in the New York Debtor and Creditor Law dealing with conveyances in fraud of creditors, enacted in 1925—3 years after the date of this lease. In that statute it is provided that insolvency means an excess of liabilities over assets. It is respectfully submitted that this statute does not represent a general New York definition of insolvency, nor is it a codification of the New York Common Law definition of insolvency, but rather one limited solely to cases involving conveyances in fraud of creditors. Consequently, petitioner's argument on this point cannot be countenanced (*In re Wil-low Cafeterias, Inc.*, 22 Fed. Supp. 617, 620; *Willcox* v. *Goess*, 16 Fed. Supp. 350, 363).

Petitioner's reference to Section 955 of the Penal Law of the State of New York regarding transactions by brokers and dealers after insolvency is not applicable to the instant case, since the Penal Law definition of insolvency is to be restricted solely to the criminal matters therein specified, and is not to be applied to civil matters and every day business transactions. Particularly is this true in the instant case involving a construction of a term used in the lease.

The contention of petitioner that the word "insolvent" as used in the lease is to be construed as referring solely to an adjudication of insolvency under the New York insolvency law as set forth in the Debtor and Creditor

Law is unsound. Assuming, *arguendo*, that the draftsman of the lease intended such, the words "in any court" following the word "insolvent" would not have been used. Rather, the draftsman would have used the words "under the laws of the State of New York". The fact that the draftsman did not use the phrase "under the laws of the State of New York" is proof that petitioner's contention is without merit.

It should not be overlooked that the debtor, Childs Company, was doing a chain store restaurant business in 1922, the date of this lease, and accordingly, the draftsman was aware of the fact that Childs Company might be involved in court proceedings in a jurisdiction other than the State of New York or the Southern District of New York. It is for this reason, and for no other, that the draftsman used the all embracing phrase "in any court".

Petitioner argues that the decision of the court below tends to defeat the very purpose of reorganization proceedings. Petitioner's argument is not novel and was rejected by this Court when advanced by counsel for the debtor in the *Wil-low Cafeterias* case when petitioning this Court for a writ of certiorari (Cert. den. *In re Wil-low Cafeterias* case, 304 U. S. 567).

It is again urged that the rule of *ejusdem generis* applies. No case is cited and the legal definition of *ejusdem generis* does not support the petitioner. The enumeration of specific things is not followed by a general word or phrase.

POINT IV

The decision of the Circuit Court of Appeals for the Sixth Circuit in *Simmons* v. *National Tool Co.*, reported in 110 Fed. (2d) 850, is not in conflict with the decision of the Circuit Court of Appeals for the Second Circuit in the instant matter, reported in 146 Fed. (2d) 594.

In the *Simmons* case the issue was the right to maintain an equity suit for damages and profits by reason of an alleged patent infringement. No forfeiture of a lease or other contract was involved.

The license agreement, after declaring National Tool Company to be the sole owner of six grinding machines, built at its own expense, with the right to use said machines in its factory at Cleveland, Ohio, states, "but the National Tool Company shall not have the right to sell or dispose of said machines directly or indirectly to any person or persons whatever, and in the event of the bankruptcy, insolvency or dissolution of the National Tool Company no title to said machines shall be vested in any receiver or trustee for purposes of using them in gear grinding shaper cutters".

There was nothing in the license to prevent the National Tool Company, the licensee, from using the machines even while involved in bankruptcy, insolvency or dissolution proceedings, or after its emergence from any such proceedings. The license agreement did not provide for forfeiture—it prohibited the sale of the machines to another or the passage of title from the licensee to any trustee or receiver.

In the instant case the court below had before it a long-term lease containing a definite and unequivocal forfeiture clause for the purpose of determining the scope of the said forfeiture clause.

The record in the *Simmons* case further indicates that Simmons and her counsel did not petition the bankruptcy court, pending reorganization proceedings, to declare a forfeiture of the license agreement, nor did they file any objections or take any exceptions to the reorganization proceedings. It should also be noted that the decree of confirmation provided, "that the status of the executory contracts of the debtor described in these proceedings and the rights, privileges and liabilities of the parties herein with respect thereto, as now existing, shall not be altered, impaired or affected by these proceedings".

The basis for the *Simmons* decision was estoppel and the word "insolvent" and the interpretation to be placed thereon was not considered by the Court.

An examination of the Simmons record indicates that any other decision by the District Court or by the Circuit Court of Appeals would have permitted Simmons to attack collaterally the concluded bankruptcy proceedings.

The Second Circuit decisions (*In re Walker*, 93 Fed. (2nd) 281; *In re Willow Cafeterias*, 22 Fed. (Supp.) 617, rev'd on another ground 95 Fed. (2nd) 306, cert. den. 304 U. S. 567) referred to by Simmons in her appeal brief were not considered by the Sixth Circuit since they were not pertinent to the issue in that case. The opinion of the Sixth Circuit does not discuss or even mention these cases.

In view of the decision of this Court in *Erie Railroad* v. *Tompkins* (304 U. S. 64) and position of counsel as stated

under Point I, the alleged conflict between the Sixth Circuit and the Second Circuit is of no moment. In *Ruhlin* v. *New York Life Insurance Company* (304 U. S. 202), this Court held:

> "As to questions controlled by state law, however, conflict among circuits is not of itself a reason for granting a writ of certiorari. The conflict may be merely corollary to a permissible difference of opinion in the state courts."

CONCLUSION.

The decision of the Circuit Court of Appeals for the Second Circuit should be affirmed.

Respectfully submitted,

BURTON C. MEIGHAN, JR.,
Counsel for Respondent.

BURTON C. MEIGHAN, JR.,
LOUIS A. MARCHISIO,
Of Counsel.

SUPREME COURT OF THE UNITED STATES.

No. 953.—October Term, 1944.

John F. X. Finn, as Trustee of Childs Company, Petitioner,
vs.
Burton C. Meighan, Jr., as Substituted Trustee Under the Last Will and Testament of William T. Wood, Deceased.

On Writ of Certiorari to the United States Circuit Court of Appeals for the Second Circuit.

[May 21, 1945.]

Mr. Justice Douglas delivered the opinion of the Court.

Childs Company operates a chain of restaurants. In August 1943 it filed a voluntary petition for reorganization under Ch. X of the Bankruptcy Act (52 Stat. 885, 886, 11 U. S. C. §§ 526, 530) alleging that it was unable to pay its debts as they matured. The petition was approved and petitioner was appointed trustee of the debtor. Childs Company had been lessee of, and had operated a restaurant on, certain premises in New York City for over forty years. Its present lease is for a term of twenty-one years ending in 1947. That lease contains the following provision:

> "The tenant covenants that . . . if a petition in bankruptcy shall be filed by the tenant or *if the tenant shall be adjudged bankrupt or insolvent by any Court*, or if a trustee in bankruptcy of the tenant shall be appointed in any suit or proceeding brought by or against the tenant, then and in each and every such case, the term hereby granted shall immediately cease, determine and come to an end, and the landlord may recover and resume possession of the demised premises by any legal means." (Italics added.)

In May 1944 petitioner advised the lessor that it desired to assume the lease. Respondent replied that the lease had ceased and come to an end by virtue of the bankruptcy proceedings. Thereafter, respondent petitioned the bankruptcy court for an order adjudging that the term granted by the lease had terminated. The court granted the relief asked by the petition. The Circuit Court of Appeals affirmed. 146 F. 2d 594. The case is here on certiorari.

The bankruptcy court does not look with favor upon forfeiture clauses in leases. They are liberally construed in favor of the bankrupt lessee so as not to deprive the estate of property which may turn out to be a valuable asset. *Gazlay* v. *Williams*, 210 U. S. 41; *Model Dairy Co.* v. *Foltis-Fischer, Inc.*, 67 F. 2d 704, 706. But an express covenant of forfeiture has long been held to be enforceable against the bankruptcy trustee. *Empress Theatre Co.* v. *Horton*, 266 Fed. 657; *Jandrew* v. *Bouche*, 29 F. 2d 346. And the 1938 revision of the Bankruptcy Act made no change in that regard. Congress granted the trustee sixty days (unless reduced or extended) in which to assume or reject a lease. § 70(b) of the Bankruptcy Act as amended, 11 U. S. C. § 110(b). But at the same time, Congress provided:

> "A general covenant or condition in a lease that it shall not be assigned shall not be construed to prevent the trustee from assuming the same at his election and subsequently assigning the same; but an express covenant that an assignment by operation of law or the bankruptcy of a specified party thereto or of either party shall terminate the lease or give the other party an election to terminate the same shall be enforceable."

This provision was merely declaratory of the law as it then existed.[1]

There is some suggestion, however, that that provision is applicable only in ordinary bankruptcy proceedings and not to reorganizations under Ch. X. It is pointed out that frequently the value of enterprises is greatly enhanced by leases on strategic premises and that if forfeiture clauses were allowed to be enforced, reorganization plans might be seriously impaired. But Congress has made § 70 applicable to reorganization proceedings under Ch. X. By § 102 (11 U. S. C. § 1002) it provided that the provisions of Ch. VII (which includes § 70) should be applicable to proceedings under Ch. X "insofar as they are not inconsistent or in conflict with the provisions" of that chapter.[2] Moreover, Congress provided in § 102 that "provisions relating to 'bankrupts' shall be deemed to relate also to 'debtors', and 'bankruptcy

[1] See 4 Collier on Bankruptcy (14th Ed. 1942), pp. 1239-1241; Weinstein, The Bankruptcy Law of 1938, p. 159.

[2] And see §§ 114 and 115. As respects the rejection or assumption of leases under Ch. X see §§ 116(1), 202, 216(4). Cf. In re Chase Commissary Corp., 11 F. Supp. 288.

But Congress has made the forfeiture provision of § 70 applicable to reorganization proceedings under Ch. X.

proceedings' or 'proceedings in bankruptcy' shall be deemed to include proceedings under this chapter." Thus we must read § 70(b) as providing that an express covenant is enforceable which allows the lessor to terminate the lease if a petition to reorganize the lessee under Ch. X is approved. Cf. *In re Walker*, 93 F. 2d 281. That being the policy adopted by Congress, our duty is to enforce it.

The question remains whether this lease should be so construed. There is to be a forfeiture "if the tenant shall be adjudged bankrupt or insolvent by any Court." It is said that "insolvent" is used interchangeably with "bankrupt". But it has long been held that a general assignment is an act of bankruptcy whether or not the debtor is insolvent. *West Co.* v. *Lea*, 174 U. S. 590. Thus it would seem that "adjudged bankrupt" and "adjudged insolvent" do not cover precisely the same ground. Moreover, insolvency in the equity sense has always meant an inability of the debtor to pay his debts as they mature.[3] Under the Bankruptcy Act it means an insufficiency of assets at a fair valuation to pay the debts. § 1(19), 11 U. S. C. § 1(19). It was long the practice to initiate reorganizations in the federal equity courts by the filing of a general creditor's bill which alleged insolvency in the equity sense.[4] There would accordingly seem to be no doubt that if a receiver were appointed pursuant to such a bill, it would bring into operation an express covenant providing for a forfeiture of a lease "if the tenant shall be adjudged insolvent by any Court." No reason is apparent why the same result should not obtain in cases of reorganization under Ch. X.

We do not believe a different result is indicated in this case merely because the provision for forfeiture on adjudication of insolvency appears in a paragraph otherwise exclusively devoted to the contingency of bankruptcy. Petitioner relies on the New York Debtor and Creditor Law, Consol. L., c. 12, which provides for the discharge of insolvent debtors in proceedings in the New York courts. §§ 50-88. It is said that insolvency under that statute means insolvency in the bankruptcy sense (§ 52) and that

[3] Glenn, Creditors' Rights and Remedies (1915), § 370.

[4] Re Metropolitan Railway Receivership, 208 U. S. 90; 1 Gerdes, Corporate Reorganizations (1936) §§ 13, 19. Part VIII, Report on the Study and Investigation of Protective and Reorganization Committees, Securities and Exchange Commission (1940), pp. 24 *et seq.*

the covenant in question was drawn so as to provide for a forfeiture in the event of such an adjudication. But as we have said, the covenant in this lease provides for forfeiture on an adjudication of insolvency "by any Court". It is difficult to see in that language a limitation of the covenant to an adjudication of insolvency by the New York courts under the Debtor and Creditor Law.[5]

Affirmed.

[5] The other provisions of New York law dealing with insolvency commonly define it as an inability to pay debts as they mature. The New York authorities are reviewed by Judge Knox in In re Schulte Retail Stores Corp., 22 F. Supp. 612, 616.